Supreme Court, U.S.
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No. _____

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1994

JESS T. SIMPSON,

Petitioner,

v.

OFFICE OF THRIFT SUPERVISION

Respondent.

On Petition for a Writ of Certiorari
to the United States Court of Appeals
for the Ninth Circuit

APPENDICES TO PETITION FOR A WRIT OF CERTIORARI

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385

TABLE OF CONTENTS

		Page
Appendix A	Opinion of Ninth Circuit Court of Appeals	A-1
Appendix B	Decision of Administrative Law Judge	B-1
Appendix C	Decision and Order of Office of Thrift Supervision	C-1
Appendix D	Order of Office of Thrift Supervision . . .	D-1
Appendix E	Order Denying Petition for Rehearing	E-1
Appendix F	Notice of Charges . . .	F-1
Appendix G	Draft Complaint	G-1

APPENDIX A

FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

JESS T. SIMPSON, former President and Chairman of the Board of Directors, Cascade Savings Bank, Everett, Washington, *Petitioner,* v. OFFICE OF THRIFT SUPERVISION, *Respondent.*	Nos. 92-70797 93-70050 OTS AP 91-6 Order No. AP 92-123 OPINION

Petition for Review of a Decision of the
Office of Thrift Supervision
United States Department of the Treasury

Argued and Submitted
March 8, 1994—Seattle, Washington

Filed July 18, 1994

Before: Procter Hug, Jr., Cynthia Holcomb Hall, and David R. Thompson, Circuit Judges

Opinion of Judge Hug

SUMMARY

Administrative Law/Adjudication/Banking

The court of appeals affirmed a decision of the Office of Thrift Supervision (OTS). The court held that administrative adjudication of a case involving alleged banking violations was not violative of the separation of powers doctrine.

Petitioner Jess Simpson was president and chairman of the board of Cascade Savings Bank, a state-chartered mutual savings and loan association. Following Simpson's resignation, an investigation raised claims of suspected impropriety against him. Respondent OTS began an investigation of Simpson, culminating in the filing of a Notice of Charges against him.

The Notice alleged that Simpson engaged in unsafe or unsound practices involving a profit-sharing plan from which Simpson improperly distributed profits to himself and other Cascade officers and managers. The Notice also alleged that Simpson breached his fiduciary duty to Cascade when he failed to disclose certain details of a loan he arranged. Finally, the Notice alleged that Simpson usurped Cascade's corporate opportunities by setting up an independent insurance agency to which commissions were diverted from Cascade's customers' purchase of mortgage life insurance. The OTS sought restitution from Simpson for the alleged violations of banking practices.

Simpson filed an answer to the Notice, and received a hearing before an administrative law judge (ALJ), who

recommended that Simpson be ordered to pay restitution for the amount Simpson distributed to himself, the amount of loss on the loan, and for all commissions paid to his insurance agency. The Director of the OTS determined that Simpson acted with "reckless disregard" not only in distributing the profit-sharing to himself, but also when he distributed profit-sharing to the other managers. The Director modified the restitution amount.

Simpson petitioned for review of the OTS's decision, challenging the administrative proceeding brought against him. Simpson contended that the separation of powers doctrine was violated by allowing a non-Article III tribunal to adjudicate his claims, and he was denied his Seventh Amendment right to a jury trial. Simpson also contended that he was

denied procedural due process of law because his case was not decided by an independent and impartial adjudicator; he argued that allowing the Director of the OTS to both issue the Notice of Charges and make the final administrative determination was impermissible. Finally, Simpson also contended that the statute of limitations barred portions of the restitution ordered, and the Director erred by concluding that he acted with "reckless disregard."

[1] Simpson's case involved the adjudication of public rights, and, accordingly, it did not violate Article III. Congress created the administrative forum to effectuate and protect the public interest. [2] The purpose of enforcement of the thrift regulation laws is to safeguard the thrift industry, the

depositors, and the federal insurance fund. By instituting the cease-and-desist proceedings, the OTS served a public purpose of the sort Congress envisioned in providing for administrative adjudication. [3] Congress' giving the OTS the authority to initiate and pursue enforcement actions did not violate Article III.

[4] Because this case involved public rights, Simpson's claimed right to a jury trial had to fail.

[5] There was no evidence that the Director was not an objective adjudicator. The Director signed the Notice of Charges, but the record did not establish that the Director thereafter acted as a prosecutor. [6] Thus, Simpson did not establish a due process violation.

[7] Because Congress provided no statute of limitation in OTS's rules and

regulations, the OTS was not time barred in asserting certain of its claims against Simpson.

[8] Substantial evidence supported the Director's decision finding "reckless disregard" on behalf of Simpson in distributing profit sharing to himself and the other managers. By improperly distributing the profits, Simpson placed Cascade's financial condition at risk.

COUNSEL

Jonathan B. Noll, Foster Pepper & Shefelman, Seattle, Washington, for the petitioner.

Kerry W. Kircher, Office of Thrift Supervision, Washington, D.C., for the respondent.

OPINION

HUG, Circuit Judge:

Petitioner Jess T. Simpson challenges the administrative proceeding brought against him by the Office of Thrift Supervision ("OTS"). On November 18, 1992, the Director of the OTS ("the Director") issued its final decision and order requiring Simpson to, among other things, pay restitution to Cascade Savings Bank for banking violations. Simpson timely petitioned for review of the Director's decision on December 7, 1992. The Director issued a second order on January 4, 1993, modifying the amount of restitution ordered. Simpson timely petitioned for review of the second order on January 27, 1993. The two petitions have been consolidated.

Simpson raises several challenges to the Director's decision. First, he raises three constitutional claims: 1) the separation of powers doctrine was violated by allowing a non-Article III tribunal to adjudicate his claims; 2) he was denied his Seventh Amendment right to a jury trial, and 3) he was denied procedural due process of law. Simpson also alleges that the statute of limitations bars portions of the restitution ordered. Finally, Simpson contends that the Director erred by concluding that he acted with "reckless disregard" or was unjustly enriched.

We have jurisdiction pursuant to 12 U.S.C. § 1818(h)(2). We conclude that Simpson's constitutional rights were not violated. Further, the restitution order was not barred by the statute of limitations, and the Director did not err

in concluding that Simpson acted with reckless disregard. Accordingly, we affirm.

I.

FACTS AND PRIOR PROCEEDINGS

Jess T. Simpson was president and chairman of the board of Cascade Savings Bank ("Cascade"), a Washington state-chartered mutual savings and loan association, from 1955 until he resigned on March 13, 1990. Following Simpson's resignation, Cascade hired K.P. Zech, of Z-Associates, Inc., to investigate Simpson. The investigation resulted in a report raising four separate claims of suspected impropriety against Simpson.

Simpson and Cascade failed to reach a settlement regarding the four claims. The OTS thereafter began an investigation of Simpson, culminating in the filing of the

Notice of Charges against Simpson on February 12, 1991. Specifically, the Notice of Charges alleged that Simpson engaged in unsafe or unsound practices and "committed acts that constitute willful disregard for Cascade's safety and soundness and breaches of fiduciary duty . . . ." The OTS sought restitution from Simpson for the alleged violations of banking practices.

The unsound practices involved a profit-sharing plan in which Simpson distributed $529,500 in profits to Cascade officers and managers, including $105,000 to himself in 1989. The 1989 final audit revealed, however, that Simpson should not have distributed any profits. The Notice of Charges also alleged that Simpson breached his fiduciary duty to Cascade when he failed

to disclose certain details to the loan committee and Board of Directors when it was approving a loan ("the Previs loan") that Simpson arranged. When the borrowers later defaulted, Cascade lost approximately $328,424 on the loan. Finally, the Notice of Charges alleged that Simpson usurped Cascade's corporate opportunities by setting up an independent insurance agency, Insurance Commerce, Inc. ("ICI"), to which commissions were diverted from Cascade customers' purchase of mortgage life insurance. ICI received approximately $161,000 in commissions. Simpson does not challenge the underlying merits of the Previs loan or the ICI commissions claims; rather, Simpson only asserts that the claims are partially barred by the applicable statute of limitations.

The OTS has authority to pursue cease-and-desist proceedings against an institution or an institution-affiliated party if, in its opinion, it has reasonable cause to believe that the institution or the institution-affiliated party has engaged, or is about to engage, in unsafe or unsound business practices, or is violating, or is about to violate, the law. *See* 12 U.S.C. § 1818(b)(1). At all relevant times, Simpson was an institution-affiliated party of Cascade in accordance with 12 U.S.C. § 1813(u).

The process begins when the OTS issues the Notice of Charges. *See* 12 C.F.R. § 509.18. After the notice issued, Simpson timely filed an answer. *See* 12 C.F.R. § 509.19(a). Pursuant to 12 U.S.C. § 1818(b)(1) and 12 C.F.R. § 505.5, Simpson received a hearing before

Administrative Law Judge Paul Cross ("the ALJ") from August 26 to August 30, 1991. The ALJ recommended that Simpson be ordered to pay restitution for the amount Simpson distributed to himself, for the amount of the loss on the Previs loan, and for all commissions paid to ICI. In addition, the ALJ imposed a $138,013 civil penalty on Simpson.

At the conclusion of the proceedings, the ALJ filed the record of the proceedings with the Director, including the ALJ's recommended decision, findings of fact and conclusions of law, as well as any transcripts, briefs, motions, rulings, etc. *See* 12 C.F.R. § 509.38. Both parties took exception to the ALJ's recommended findings of fact and conclusions of law. The Director of the OTS reviewed the complete record and

issued its final decision and order. The Director determined that Simpson acted with reckless disregard not only in distributing the profit-sharing to himself, but also when Simpson distributed profit-sharing to the other managers. The Director increased the restitution amount to $1,009,446, taking into account the entire amount of profit-sharing Simpson approved and distributed. However, the Director reversed the ALJ's civil penalty assessment. After learning that Cascade's Board of Directors removed $105,000 from Simpson's account, the Director issued a second order reducing the ordered restitution by that amount. The Director's decision is reviewable by our court pursuant to 12 U.S.C. § 1818(h)(2).

II.

SEPARATION OF POWERS

Simpson contends that the adjudication of his case by a non-Article III tribunal violated the separation of powers doctrine provided by the United States Constitution. This claim must fail.

"On its most fundamental plane, the separation of powers doctrine protects the whole constitutional structure by requiring that each branch retain its essential powers and independence." *Pacemaker Diagnostic Clinic of America v. Instromedix*, 725 F.2d 537, 544 (9th Cir.) (en banc), *cert. denied*, 469 U.S. 824 (1984). It is a well-settled rule that "[t]he judicial power of the United States must be exercised by courts having the attributes prescribed in Art. III."

Northern Pipeline Co. v. Marathon Pipeline Co., 458 U.S. 50, 59 (1981) (plurality). Article III, section 1 of the United States Constitution provides:

> The Judges, both of the supreme and inferior Courts, shall hold their Offices during good Behavior, and shall, at stated Times, receive for their Services, a Compensation, which shall not be diminished during their Continuance in office.

A line of cases has developed, however, which excepts certain actions from Article III adjudication. Historically excluded from Article III adjudication are cases in territorial courts, court-martials, and cases adjudicating public rights. *Northern Pipeline*, 458 U.S. at 64-67. The only applicable exception to this case is the public rights doctrine.

Simpson asserts that his case does not involve public rights, but rather, it essentially involves masqueraded state law

claims that could have been asserted by Cascade. Thus, he argues, adjudication by a non-Article III judge violated the separation of powers doctrine. We reject at the outset Simpson's claim that the OTS acted in essence on behalf of Cascade in pursuing a damages claim recoverable under common law. The OTS acted independently pursuant to its congressionally mandated authority under 12 U.S.C. § 1811 *et seq.* Accordingly, we next address whether this case involves public rights.

Although there is no bright-line rule detailing what constitutes a public rights case, the plurality of the Supreme Court in *Northern Pipeline* stated that the exception only extends to "matters arising 'between the Government and persons subject to its authority in connection with the performance of the constitutional

functions of the executive or legislative departments,' and only to matters that historically could have been determined exclusively by those departments." *Id.* at 67-68 (citations omitted). The plurality held that Article III bars Congress from providing Article I bankruptcy courts with jurisdiction over all matters arising under the bankruptcy laws. *Id.* at 85, 87 (jurisdiction which extended to "all civil matters arising under Title III or arising in or *related to* cases under Title III" was improper).

The Supreme Court later revisited the public rights exception in *Commodity Futures Trading Commission v. Schor*, 478 U.S. 833 (1986). In reviewing Article III challenges, the Court noted that it weighs a number of nondeterminative factors, including "the extent to which the

'essential attributes of judicial power' are reserved to Article III courts, and, conversely, the extent to which the non-Article III forum exercises the range of jurisdiction and powers normally vested only in Article III courts, the origins and importance of the right to be adjudicated, and the concerns that drove Congress to depart from the requirements of Article III." *Id.* at 851 (citations omitted). In *Schor*, the Court held that the Commodity Futures Trading Commission could entertain limited jurisdiction over state law counterclaims in reparation proceedings without violating Article III. *Id.* at 857.

[1] Against this backdrop, we conclude that Simpson's case involved the adjudication of public rights, and accordingly, it did not violate

Article III. Examination of the congressional scheme in light of the above factors establishes that Congress created the administrative forum to effectuate and protect the public interest.

[2] The purpose of enforcement of the thrift regulation laws is to safeguard the thrift industry, the depositors, and the federal insurance fund. Simpson's claim that Cascade remained solvent at all times is inapplicable. Insolvency is not required. The unsound business practices committed by Simpson threatened Cascade's solvency by improperly dissipating its assets, thereby weakening its financial stability and undermining the interests and confidence of Cascade's depositors. Thus, the OTS instituted this action to protect those interests and to prevent and/or stop unlawful practices. By

instituting the cease-and-desist proceedings, the OTS served a public purpose of the sort Congress envisioned in providing for administrative adjudication. *See Akin v. Office of Thrift Supervision*, 950 F.2d 1180, 1186 (5th Cir. 1992); *Paul v. Office Thrift Supervision*, 763 F. Supp. 568, 573-74 (S.D. Fla. 1990) (enforcement proceedings under 12 U.S.C. § 1811 *et seq.* is an action to enforce public rights), *aff'd without opinion*, 948 F.2d 1297 (11th Cir. 1991).

[3] Finally, Congress provided adequate and meaningful judicial review by a United States Court of Appeals pursuant to 12 U.S.C. § 1818(h)(2). Thus, Simpson is entitled to, and is receiving, Article III appellate review. That Congress intended to give the OTS the power and authority to initiate and pursue

enforcement actions is clear from the terms of 12 U.S.C. § 1818 and the accompanying regulations. This grant of authority does not violate Article III.

III.

JURY TRIAL

[4] We review *de novo* the legal question whether Simpson was entitled to a jury trial in federal court. *Securities and Exchange Comm'n v. Rind*, 991 F.2d 1486, 1493 (9th Cir.), *cert. denied*, 114 S. Ct. 439 (1993). Because we conclude that this case involves public rights, Simpson's claimed right to jury trial must also fail.

The Seventh Amendment provides that "[i]n Suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved." U.S. Const. amend. VII.

The Supreme Court has consistently interpreted "Suits at common law" to refer to "suits in which *legal* rights were to be ascertained and determined, in contradistinction to those where equitable rights alone were recognized, and equitable remedies were administered." *Granfinanciera S.A. v. Nordberg*, 492 U.S. 33, 41 (1989). Furthermore, in cases in which "'public rights' are being litigated,—e.g., cases in which the Government sues in its sovereign capacity to enforce public rights created by statutes within the power of Congress to enact—the Seventh Amendment does not prohibit Congress from assigning the factfinding function and initial adjudication to an administrative forum with which the jury would be incompatible." *Atlas Roofing Co. v.*

Occupational Safety and Health Review Comm'n, 430 U.S. 442, 450 (1977).

Although this circuit has not addressed this particular issue, the Fifth and Eleventh Circuits have found that the right to a jury trial in an OTS proceeding is not violated because the OTS's action is an enforcement of public rights. *See Akin*, 950 F.2d at 1186 (5th Cir. 1992)("Where there is a proper administrative forum for adjudicating public rights, there is no right to a jury trial."); *Paul*, 763 F. Supp. at 573-74 (plaintiff claimed that OTS action was tantamount to an action for damages; court disagreed finding no Seventh Amendment violation because case involves public rights).

Simpson argues that this case is really a claim for damages and is

therefore legal in nature deserving of a jury trial. Simpson's contention is unpersuasive. This case involves an order of restitution, an equitable remedy. Merely because this case involves a claim for restitution of money does not detract from its equitable nature. *See Rind*, 991 F.2d at 1493; *see also Federal Sav. & Loan Ins. Corp. v. Dixon*, 835 F.2d 554, 561 (5th Cir. 1987)(in suing for restitution of funds milked from bank, FSLIC is pursuing an equitable remedy).

We conclude that the Seventh Amendment is inapplicable to this OTS proceeding which implicates public rights. As discussed above, Congress provided Simpson a proper administrative forum for adjudicating this action. Therefore, Simpson was not denied his Seventh Amendment right to trial by jury.

IV.

PROCEDURAL DUE PROCESS

Simpson contends that he was denied due process of law because his case was not decided by an independent and impartial adjudicator. He asserts that the procedural makeup of the proceedings, in which the Director of the OTS both commences the proceedings by issuing the Notice of Charges and makes the final administrative determination, is impermissible.

"[T]he combination of investigative and adjudicative functions does not, without more, constitute a due process violation." *Withrow v. Larkin*, 421 U.S. 35, 58 (1975). The Court, however, may determine that special facts and circumstances in the case warrant a due

process evaluation because "the risk of unfairness is intolerably high." *Id.*

Simpson's claim that the Director formed an opinion on Simpson's case before final adjudication does not stand up. Although the Director signed the Notice of Charges, the charges do not establish a personal opinion on behalf of the Director. Rather, the charges state that *the OTS*, an administrative agency, is of the opinion that Simpson violated the Savings Associations Rules and Regulations. Although the Director is the head of the OTS, his participation at the commencement of the proceedings is minimal.

A charge may not be filed until the OTS, "upon due deliberation, determines that continued service or participation by the individual may pose a threat to the

interests of the association's depositors or may threaten to impair public confidence in the association." 12 C.F.R. § 508.3(a). But the issuing of charges is only the beginning of the proceedings. The Director does not investigate or prosecute the case. In fact, all interested parties are forbidden from ex parte communication with the Director. The regulation provides:

> From the time the notice is issued by the Director until the date that the Director issues its final decision . . ., no party, interested person or counsel therefor shall knowingly make or cause to be made an ex parte communication concerning the merits of the proceeding to the Director, the administrative law judge, or a decisional employee.

12 C.F.R. § 509.9(b).

[5] The system is not a perfect one. Certainly, when the Director signs the charges and thereafter makes the decision

on the charges, it exudes a possible appearance of impropriety. However, there is no evidence that the Director is not an objective adjudicator. The Director signed the Notice of Charges in a quasi-judicial fashion, authorizing the institution of proceedings. The record does not establish that the Director thereafter acted as a prosecutor. The cases cited by Simpson in which a due process violation occurs if the prosecutorial and adjudicative functions are combined in one individual are inapposite. The actual prosecution of Simpson's case was handled by attorneys from the Enforcement Division of the Chief Counsel's Office who were prohibited from ex parte communication with the Director.

[6] Furthermore, the statute provides that Simpson is entitled to a hearing

before an ALJ before it reaches the Director for review. Simpson makes no claim that the ALJ was biased. It was not until after Simpson's hearing was held before the ALJ that the case came before the Director for review. On review, the Director exhibited his objectivity and neutrality by reversing the civil penalties assessed against Simpson. Finally, even after the Director made his determination on review, the case is then subject to appellate review by an Article III court. Simpson has not established a due process violation.

V.

STATUTE OF LIMITATIONS

Simpson contends that portions of the OTS's restitution claims are time barred. There is no federal statute of limitation specifically applicable to the OTS's

action under 12 U.S.C. § 1818. If Congress has not provided an applicable statute of limitation, generally, the United States is not subject to a statute of limitation in enforcing its rights. *See Donovan v. West Coast Detective Agency, Inc.*, 748 F.2d 1341, 1343 (9th Cir. 1984); *United States v. Tri-No Enters., Inc.*, 819 F.2d 154, 158 (7th Cir. 1987).

[7] Because we conclude that Congress provided no statute of limitation in OTS's rules and regulations, we hold that the OTS is not time barred in asserting the restitution claims against Simpson involving the Previs loan and the ICI commissions.

VI.

SUBSTANTIAL EVIDENCE

Simpson's final contention is that the Director erred in ordering Simpson to pay restitution. We must sustain the Director's findings if they are supported by substantial evidence in the record as a whole. *del Junco v. Conover*, 682 F.2d 1338, 1340 (9th Cir. 1982), *cert. denied*, 459 U.S. 1146 (1983); *Akin*, 950 F.2d at 1183.

Title 12 U.S.C. § 1818(b)(1) permits the OTS to issue a cease-and-desist order if an institution-affiliated party is engaging or has engaged in various proscribed activities, including engaging in an unsafe or unsound practice in conducting the business of the depository institution. An unsafe or unsound practice is one "which is contrary to

generally accepted standards of prudent operation, the possible consequences of which, if continued, would be abnormal risk or loss or damage to an institution, its shareholders, or the agencies administering the insurance funds and that it is a practice which has a reasonably direct effect on an association's financial soundness." *Hoffman v. FDIC*, 912 F.2d 1172, 1174 (9th Cir. 1990)(citations and quotations omitted). The OTS is given a wide range of affirmative action it may take, including ordering restitution or taking any other action it deems appropriate. *See* 12 U.S.C. § 1818(b)(6)(A-F).

The Director ordered Simpson to pay restitution. Restitution is an appropriate remedy under two circumstances: 1) if the depository

institution or the party was unjustly enriched in connection with the violation or practice, or 2) if the violation or practice involved a reckless disregard for the law or any applicable regulations or prior order. 12 U.S.C. § 1818(b)(6)(A)(i-ii). The statute does not define either "unjust enrichment" or "reckless disregard."

In determining that Simpson acted with reckless disregard, the Director looked to the meaning of "reckless" in other statutory schemes. For the purposes of 12 U.S.C. § 1818(b)(6)(A)(ii), the Director concluded that reckless disregard for the law exists when:

> (1) the party acts with clear neglect for, or plain indifference to, the requirements of the law, applicable regulations or agency orders of which the party was, or with reasonable diligence should have been, aware; and

> (2) the risk of loss or harm or other damage from the conduct is such that the party knows it, or is so obvious that the party should have been aware of it.

In reviewing an agency's construction of a statute, we must reject constructions that are contrary to clear congressional intent or frustrate the policy that Congress sought to implement. *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843 n.9 (1984). If the statute is silent or ambiguous on a particular point, we defer to the agency's interpretation. *Id.* at 843.

[8] We conclude that the Director's interpretation is a permissible construction of the statute. Applying the Director's definition of reckless disregard, we hold that substantial evidence supported the Director's decision finding reckless disregard on behalf of

Simpson in distributing profit sharing to himself and the other managers. By improperly distributing the profits, Simpson placed Cascade's financial condition at risk. This court recently found compelling the argument that restitution in an OTS enforcement action "may not only compensate an institution for past wrongs, but [it] may also serve to prevent the dissipation of assets that may belong to it, and thereby prevent prejudice to its depositors." *Spiegel v. Ryan*, 946 F.2d 1435, 1438 (9th Cir. 1991), *cert. denied*, 112 S. Ct. 1584 (1992).

Simpson distributed the profit sharing pursuant to a profit-sharing plan under the Board of Directors' control. At the end of each year, one-half of all profits above the "target" were available for distribution. The 1989 target was

$2 million. Simpson determined on December 31, 1989 that $529,500 would be distributed pursuant to the profit-sharing plan. From this amount, Simpson received $105,000. The remainder was distributed to 26 other Cascade officers and managers.

After Simpson's resignation, the final 1989 audit came out showing a net profit of only $918,667;[1/] thus, Cascade did not even reach its target amount. Based on this audit, Simpson should not have authorized or distributed any profits. At the time Simpson made the distributions, Simpson contends that there was confusion as to the true financial condition of Cascade. The primary dispute was over write-downs. However, recognizing that a dispute existed over

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[1/]This figure does not include the profit-sharing distribution.

the write-downs, Simpson should not have authorized distribution of profit-sharing. At the very least, in light of the uncertainty, Simpson should have waited until the final audit to authorize distribution.

In addition, at the time of the distribution, the record establishes that Cascade was not in compliance with the Financial Institutions Reform, Recovery and Enforcement Act capital requirements. Although Cascade was working under an OTS approved capital plan at all relevant times, Simpson was aware that any money distributed would not increase Cascade's capital position. Finally, Cascade did not meet the general loan loss reserve requirements. Although Simpson was aware that Cascade needed to have a loan loss reserve, he failed to create it prior to

distributing the profit sharing. The Director concluded that Simpson breached his fiduciary duty and duty of loyalty to Cascade by engaging in activity that promoted his own interest and that could lead to a conflict of interest. We hold that the Director's decision is supported by substantial evidence.

AFFIRMED.

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APPENDIX B

UNITED STATES OF AMERICA
Before the
OFFICE OF THRIFT SUPERVISION
DEPARTMENT OF THE TREASURY

In the Matter of JESS T. SIMPSON, Former President and Chairman of the Board of Directors Cascade Savings Bank Everett, Washington	**Re: OTS AP 91-6** **Dated: February 12, 1991**

DECISION

By Paul S. Cross, Administrative Law Judge

Teresa Hennessy and Timothy P. Leary for Enforcement, Office of Thrift Supervision.

Jonathan B. Noll for Respondent.

Scott A. Miburn, in a limited appearance, for Cascade Savings Bank.

Cease and desist order requiring restitution entered. Order of prohibition, and order for civil money penalty also entered.

Respondent ordered to pay restitution of $594,946 and Civil Money penalty of $138,013.

STATEMENT OF THE CASE

The Office of Thrift Supervision ("OTS") pursuant to a Notice of Charges and Hearing ("Notice") issued on February 12, 1991 by Director of OTS ("Director") seeks an Order to Cease and Desist Directing Restitution and Other Affirmative Relief, an Order to Prohibit, and an Order Assessing a Civil Money Penalty, against the Respondent, Jess T. Simpson, former President and Chairman of the Board of Directors of Cascade Savings Bank, Everett, Washington ("Simpson").

In its Notice OTS asserts facts concerning four separate transactions which, either individually or taken together, are alleged to provide sufficient grounds for the issuance of the requested orders. (Through

stipulation, one of the four transactions was deleted.)

As to the first of the three remaining transactions, OTS alleges in the Notice that Simpson improperly distributed $529,500[1/] at year-end 1989 pursuant to a profit-sharing plan in force at Cascade at that time. Simpson received $105,000 of this amount, with the remainder going to approximately 26 other Cascade officers and managers. OTS asserts that such conduct requires the issuance of an Order to Cease and Desist, directing restitution by Simpson to Cascade of the $529,500, an Order of Prohibition, and an order Assessing a Civil Money Penalty.

[1/]The Notice indicates approximately $530,000.

In the second of these transactions, OTS alleges in the Notice that Simpson received a loan procurement fee, in violation of 12 C.F.R. §§ 563.40, when assertedly he caused Cascade to loan money to Randy S. Previs in return for Mr. Previs's purchase of Simpson's yacht. After at least two extensions were made on this loan, the property was foreclosed, and Cascade assertedly lost funds[2/]. OTS alleges that this conduct requires issuance of an order to Cease and Desist, directing restitution, and an Order of Prohibition.

In the alternative, OTS alleges in the Notice that Simpson failed to disclose material facts concerning the

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[2/]The Notice specifies the amount of the loss as approximately $238,000, but subsequently herein the loss is computed as $328,424.

loan and Simpson's relationship with Mr. Previs to Cascade's Board of Directors prior to the Board's approval of the original loan and its extensions. OTS alleges that such conduct requires the issuance of an order to Cease and Desist, directing restitution and an Order of Prohibition.

In the third of the involved transactions, OTS alleges in the Notice that Simpson operated a privately-owned corporation, Insurance Commerce, Inc. ("ICI"), which received commissions from insurance payments made by borrowers of Cascade to a local life insurance company, Family Life Insurance Company ("Family Life"). The Notice also alleges that ICI received commissions as a result of the placement of Cascade's own insurance by a local insurance broker,

Worthington Insurance Company ("Worthington"). Through these two arrangements, ICI received $161,423[3/] from on or about January 1, 1981 through May 10, 1990. OTS alleges that such arrangements require the issuance of an Order to Cease and Desist, directing restitution of $161,423, an Order of Prohibition and an Order Assessing a Civil Money Penalty.

In the alternative, OTS alleges in the Notice that Simpson failed to disclose material facts concerning ICI's operations and his relationship with ICI to Cascade's Board of Directors, thereby preventing and discouraging any Board consideration or decision whether to create a subsidiary similar to ICI. OTS

[3/]The Notice indicates at least $161,000, but subsequently herein the amount is quantified as $161,423.

alleges that such asserted conduct also requires issuance of an Order to Cease and Desist, directing restitution of $161,423, an Order of Prohibition an order Assessing a Civil Money Penalty ("CMP").

The sum total of the civil money penalty which OTS seeks to assess is $134,013[4/], representing essentially the asserted amount of gain Simpson realized as a result of the alleged violations, unsafe or unsound practices, or breaches of fiduciary duty which occurred after the passage of the Financial Institutions

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[4/]The Notice does not break out the various components of the civil money penalty ("CMP") but it consists of $105,000 for the 1985 profit sharing distribution to Simpson, a conservative estimate of $13,013 ICI funds received by Simpson or his family after August 9, 1989 and $20,000 in OTS investigative costs.

Reform, Recovery and Enforcement Act of 1989 ("FIRREA"). (The total also includes an amount for the cost of the investigation of OTS.) In addition to the civil money penalty, OTS also seeks, as noted, restitution by Simpson to Cascade on account of the three transactions in the total amount of $1,019,000. (The exact non-rounded total appears to be $1,018,847.)

Simpson filed a timely answer to the Notice, requested a hearing, and asserted several affirmative defenses. On March 28, 1991, OTS filed a motion to strike the affirmative defenses advanced by Simpson in his Answer. (In effect, OTS sought summary judgement on the affirmative defenses.) Because of the size of the CMP and restitution sought from Simpson and because the issues are

novel, a ruling on the OTS motion was held in abeyance pending factual development of the case. With the written post-hearing submissions, the motion is now ripe for decision and is dealt with in a next section of this decision. As it turns out, the affirmative defenses mostly are issues of law.

In conjunction with the Notice issued February 12, 1991, the Director also issued a Temporary Order to Cease and Desist, specifying certain actions which Simpson is to take and to cease from taking. Through various submissions, including letters and an affidavit, Simpson is in compliance with the Temporary Order. (OTS informed Simpson of its position that he is in compliance by letter dated April 1,

1991.) As part of this compliance, Simpson posted approximately $950,000 security against any judgment OTS may receive.

A hearing on the charges contained in the Notice was held before this Administrative Law Judge, between August 26 and August 31, 1991, at Seattle, Washington.[2/] At that time, both OTS and

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[2/]Simpson requested a hearing on the civil money penalty assessment pursuant to 12 U.S.C. §§ 1818(i)(2)(H). The hearing thereon was consolidated with the hearing on the underlying charges contained in the Notice. Because this proceeding arises under the Administrative Procedure Act, and because at the time of Notice, OTS did not have its own Administrative Law Judges, the United States Office of Personnel Management ("OPM") approved a "loan" of this Administrative Law Judge to OTS for this case. OTS concurred in that assignment but it was OPM and not OTS which made the assignment. Presumably, OTS retained some residual authority over the assignment but there is no indication that the OPM action designating a specific Administrative Law Judge was

(continued...)

Simpson presented testimony and documents. As mentioned, prior to the hearing, OTS and Simpson resolved one of the four charges. That charge specified in paragraphs 44-47, involving educational expenses, is withdrawn. Opening briefs and proposed findings of fact and conclusions of law were filed by the parties pursuant to 12 C.F.R. §§ 509.27. Reply briefs also were filed by the parties. A request, but not an order, was made by the ALJ that the post-hearing briefs be filed in the form of word processing diskettes, in addition to the mandatory hard copies (printed pages). Without objection, such was done. Use of such diskettes is a sound practice and is employed by many ALJ's to

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[2/](...continued)
influenced by OTS.

excellent advantage. Such use, especially in complex cases with decisional time constraints, reduces clerical "down-time" and provides more time for work on substantive issues. Also, in banking cases such as this, there is a vast amount of underlying fact which is necessary to the case but is not disputed. Use of diskettes allows for careful exposition of the record in a highly professional manner without retyping of undisputed facts. At the same time, hundreds or thousands of changes, deletions, additions or modifications are readily incorporated into an ALJ's statement of facts through the use of computer diskettes.

PROCEDURAL MATTERS

Simpson raises various Affirmative Defenses. These are the subject of an

OTS Motion to Strike Affirmative Defenses. Basically, respondent takes the view that OTS has no statutory or constitutional authority to seek restitution to Cascade of funds or benefits received by Simpson which according to OTS belong to Cascade, not Simpson. Respondent asserts he has a right to a jury trial under the Constitution of the United States. He also says that this proceeding violates his right to due process under the Fifth Amendment to the Constitution. He further asserts that he cannot be charged under the Financial Institution Reform Recovery and Enforcement Act of 1989 ("FIRREA") as to any event occurring before the August 9, 1989 effective date of FIRREA. Such, according to Simpson, would constitute ex post facto

enforcement of law in violation of the Constitution. Respondent further asserts that review of the Previs and ICI matters are time barred by applicable statutes of limitations. Argument additionally is made that Cascade is solvent and is the real party in interest, not OTS. Simpson says that the claims herein made, if at all by Cascade in the U.S. District Court for the Western District of Washington or in the courts of the State of Washington. Finally, respondent asserts that the civil money assessment was made unlawfully prior to hearing and that it is not established by a formula.

Basically, the affirmative defenses raise legal issues and except for occasional comments and arguments were not a significant feature of the evidentiary hearing. However, additional

arguments are on these issues are presented by respondent in his opening post-hearing brief and such arguments are next considered.

The first affirmative defense is that a hearing for an order to cease and desist for restitution and for assessment of a civil money penalty violates Simpson's right to trial pursuant to Article III of the Constitution of the United States. Article III sets out the broad parameters of Federal court jurisdiction. In part, Article III provides that "[t]he judicial Power shall extend to . . . controversies to which the United States shall be a party."

Under 12 U.S.C. §§ 1818(b), (e) and (i)(2), Simpson is entitled to an administrative hearing. Further, 12 U.S.C. §§ 1818(h)(2) provides that an

aggrieved party may appeal a final decision of OTS to the United States Court of Appeals for the district where the association is located. Simpson is thus afforded review in a Federal court. The Supreme Court has held in various cases that Congress is not barred from acting pursuant to its powers under Article I to vest decision making authority in tribunals that lack the attributes of Article III courts.

Simpson's second affirmative defense attacks the kind of hearing provided on the cease and desist order and the assessment of a civil money penalty as being in violation of his right to due process guaranteed by the Fifth Amendment to the Constitution of the United States. The conduct of the hearing provided by 12 U.S.C. §§ 1818(b), (e) and (i) is

governed by 12 C.F.R. § 509.24. OTS regulations provide that all hearings shall be conducted in accordance with Chapter 5 of the Administrative Procedure Act ("APA), 5 U.S.C. § 501, et seq. See 12 C.F.R. § 509.24. The procedures described in § 509.24 satisfy the due process requirements of the Fifth Amendment, as well as § 554 of the APA.

It is generally recognized that the Fifth Amendment requirement of due process applies to the conduct of administrative agencies and officials. See Morgan v. U.S., 304 U.S. 1, 19-20 (1937).

Due process requires a reasonable opportunity to know the claims of the opposing party and to meet them. It also is important that when governmental agencies adjudicate or make binding

determinations which directly affect the legal rights of individuals, procedures be used which have traditionally been associated with the judicial process.

FIRREA requires that a respondent receive a Notice of Charges specifying the grounds for the remedies sought at least 30 days prior to a hearing such as was done here. Also, OTS procedures at 12 C.F.R. 509.24 specifically provide that "[e]very party shall have the right to present its case or defense by oral and documentary evidence and to conduct such cross-examination as may be required for full disclosure of the facts." Section 509.24 further provides parties the opportunity to object to the admission or exclusion of evidence and to seek rulings on such objections on the record. It also is required that formal

proceedings be recorded and a copy of the transcript be provided to any party on request. OTS rules also allows the Administrative Law Judge to grant continuances or time extensions for good cause and allow the Administrative Law Judge to call for the productions of further evidence upon any issue, permit oral argument and the submission of briefs at or following the hearing, and reopen the hearing at any time prior to the filing of his recommended decision.

Such rules and a proceeding thereunder conforms with the requirements of the APA at 5 U.S.C. § 554. That section requires timely notice, opportunity for all interested parties to submit facts, arguments, offers of settlement and an impartial decisionmaker such as an Administrative Law Judge

appointed under the APA. The hearing herein meets these requirements.

Simpson next objects that the hearing on the cease and desist order for restitution and the assessment of a civil money penalty violates his right to a jury trial. However, Congress may create causes of action involving public rights free from jury trial requirements.

The present proceeding involves public rights. This action was brought by OTS in its role as regulator of federally-insured depository institutions, against an individual affiliated with such an institution, for alleged violations committed in that individual's role as president and chairman of such an institution. This proceeding involves a federal regulator

and an individual subject to the jurisdiction of that regulator.

In his fourth affirmative defense, Simpson argues that FIRREA is only effective with regard to matters occurring after its effective date, August 9, 1989. As such, Simpson concludes that "[t]he enforcement of any proceeding, rule or regulation, or penalty established pursuant to FIRREA for any acts or omissions occurring prior to August 9, 1989 constitutes ex post facto enforcement of law in violation of Simpson's rights guaranteed by the Constitution of the United States. Of course, since the civil money penalty assessment contained in the Notice is based entirely on asserted violations and practices which occurred after the enactment of FIRREA, this penalty portion

of the proceeding does not violate the ex post facto clause of the Constitution. In addition, the portions of this proceeding dealing with the proposed cease and desist order, restitution and the proposed prohibition order also do not violate the ex post facto clause of the Constitution.

The prohibition against the passage of an "ex post fact law" is confined to penal legislation which imposes or increases criminal punishment for conduct lawful previous to its enactment. Moreover, prior to the enactment of FIRREA, the Federal Home Loan Bank Board, the predecessor agency to the OTS, had substantially similar enforcement authority to that presently possessed by the Director of OTS to institute cease and desist proceedings and prohibition

procedures against any officer, director, employee, agent or other person participating in the conduct of the affairs of a savings association. See §§ 407(e) and (g) of the National Housing Act ("NA"), formerly 12 U.S.C. §§ 1730(e) and (g) (1982) and 12 U.S.C. § 1464(d)(1) (1982). As a result of FIRREA's enactment, the authority to enforce these provisions is granted to OTS pursuant to Section 5(d)(1)(A) of the Home Owners Loan Act ("HILA"), as amended by Section 301 of FIRREA, 12 U.S.C. § 1464(d)(1)(A).

In particular, the predecessor statutory provision under 12 U.S.C. § 1730(e) (1982) permitted the Federal Savings and Loan Insurance Corporation ("FOLIC") to require a party to "correct the conditions resulting from any . . .

violation or practice," which could include an order the payment of restitution. Such action is remedial not punitive.

Simpson's fifth affirmative defense states that since Cascade and its attorneys were aware of the circumstances involving the Previs loan no later than 1983, "all proceedings regarding that matter are barred by the applicable statute of limitations." However, there is no state statute of limitations that applies to OTS even though a beneficiary of the OTS action would include Cascade which is subject to a statute of limitation. OTS does not "stand in the shoes" of Cascade and as a matter of fact did not itself discover the existence of the Previs transaction until 1989. OTS is not time barred by Federal statute.

Simpson's sixth affirmative defense states that portions of the matters alleged with regard to Simpson's usurpation of a Cascade business opportunity and Simpson's improper billing of personal expenses also "are barred by the applicable statute of limitations." The discussion above, dealing with Simpson's fifth affirmative defense, suffices for Simpson's sixth affirmative defense.

In his seventh affirmative defense, Simpson raises the argument that since Cascade is a solvent institution, the allegations stated in the Notice "are the property of Cascade, and Cascade is the real party in interest." This defense continues: "OTS and any other state or federal regulators are not the real parties in interest and have no authority

to pursue the claims set forth in the Notice of Charges. The prosecution of the claims set forth in the Notice of Charges must be made, if at all, by Cascade in the United States District Court for the Western District of Washington or in the courts of the State of Washington."

There are no provisions in FIRREA, nor in any of FIRREA's predecessor statutes, requiring that an institution be a party to an action brought by OTS pursuant to its regulatory authority, whether the institution is solvent or not. OTS has independent authority to enforce the banking laws and regulations which is not dependent upon whether Cascade determines to initiate its own action. It is true that an attorney for Cascade made an appearance at the hearing

and was in constant attendance. Occasionally, he provided "notes" to counsel for OTS. However, Cascade did not become a full party to the proceeding (TR 23-24) and except for occasional note passing by Cascade counsel to OTS counsel, did not participate in the hearing.

Simpson's eight affirmative defense attacks the amount and computation of the civil money penalty assessment (sometimes referred to as "CMP") contained in the Notice.

The civil money penalty assessment refers to the amount of money Simpson received after the effective date of FIRREA as a result of the asserted improper actions detailed in the Notice. That sum, plus the cost to the United States of the investigation, make up the

assessed penalty. It is intended as a punishment and might well have been set at a higher or lower figure. The matching of benefits received by Simpson with the amount of the proposed penalty is not without a rational basis as is subsequently explained.

As well, the fact that the assessment was made prior to a hearing does not violate Simpson's Fifth Amendment due process rights. Simpson is in the process of a hearing with appeal rights on the assessment. The merits of and amount of the assessment are to be determined in this matter.

In his ninth affirmative defense, Simpson argues that the assessment of a civil money penalty prior to a hearing is arbitrary and capricious, but such is not

a final conclusion of OTS, as is noted above.

Simpson next objects that the amount of the civil money penalty bears no relationship to the asserted harm to Cascade. However, as will be shown, the penalty corresponds to the gain Simpson realized, as a result of the asserted practices detailed in the notice which occurred after August 9, 1989. The total amount also includes $20,000, a conservation of the total cost of this investigation. The total amount has a direct relationship to the asserted loss suffered by Cascade, the asserted gain realized by Simpson, and the cost of investigation incurred by OTS.

All things considered, the affirmative defenses of Simpson are not well taken and are rejected, except that

the subject of the CMP is later dealt with herein on the merits, rather than from the procedural point of view taken in the above discussion.

Other procedural objections raised by Simpson are that for the purpose of this proceeding, the Administrative Law Judge is an employee of OTS. The Administrative Law Judge is required by and in fact enabled by the APA to make decisions independently of the enforcement component of OTS. However, the ALJ must also follow lawful OTS policy. This latter requirement does not violate the due process rights of Simpson. Even the Federal courts are required under the so-called Chevron doctrine to respect lawful OTS policy. At the same time, OTS itself is required to respect the independence conferred

upon ALJ's by the APA, and cannot summarily dismiss detailed findings of an ALJ even under a standard of "de novo" review such as is possessed by OTS.

The evidentiary record in this matter essentially was completed upon the closing of the oral hearing on August 31, 1991. However, final post-hearing briefs were not dated and sent for filing until November 18, 1991. Meanwhile, Congress enacted new banking legislation. By order dated December 10, 1991, I reopened the record to request the statements of the parties relative to the relevance of the new legislation of Congress. A statement was received from respondent on December 16, 1991, to the effect that the Federal Deposit Insurance Act of 1991 is not relevant to the instant matter.

STATEMENT OF FACTS AND CONCLUSIONS[6/]

[6/]It is the practice of most Federal agencies to employ a "narrative" decisional format. This provides for a fair understanding of substantive as opposed to technical aspects of a proceeding. The Federal banking agencies, along with a few other agencies such as BATF frequently use a numbered format for findings of fact and conclusions of law. The format is often not unlike that of a chronology which aids understanding but tends to bury important substance within a long listing of lesser facts and circumstances. The genesis of a decision by the numbers is not clear but it does appear that Examiners for the Federal banking agencies maintain a numbered chronology where there is potential for significant enforcement action. Possibly, because the basic findings already have been composed in numbered fashion by an examiner, Enforcement counsel use the same method. Whatever, the traditional decisional format of the banking agencies certainly satisfies the APA, but it is not necessarily the best method. Over the years, this ALJ has favored a narrative decision as opposed to one with numbered findings. However, when deciding banking cases, I have combined the two methods using both a narrative and numbered findings (the latter usually in an appendix or appendices). In so doing, the intent is to conform to practice of the banking agencies while

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1989 Profit Sharing Distribution

The dispute over 1989 profit sharing is important because non-distributed profits go to a retained earnings account and add to capital. Cascade was not in capital compliance in 1989. Nonetheless, Simpson approved a distribution of $529,000 in 1989 profits, including $105,000 to Simpson. In order to make any distribution, Cascade required 1989 profits in excess of $2 million. Actual profits were less than $1 million. Simpson had reason to believe in 1989 that 1989 profits were less than $2 million and that profit sharing was impossible. Thus, OTS attacks the distribution as being in reckless

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[6/](...continued)
providing a substantive description of the decisional basis.

disregard of Simpson's fiduciary duty to Cascade.

OTS shows that Cascade was informed in 1989 that its capital was inadequate under new standards required by FIRREA. However, Cascade met two of the three new capital standards (Thorkildsen, TR 55). Further, Congress contemplated that many savings institutions would not immediately meet the new capital standards, and provided that they could submit plans to bring their capital into compliance over a period of time. FIRREA, § 301(5)(t)(6), 12 U.S.C. § 1464(t)(6). Cascade timely submitted a capital plan, which was approved (Thorkildsen, TR 68).

Of course, the profit sharing plan provided for a distribution based upon net income, not capital. Although there

were concerns regarding Cascade's capital, Cascade's 1989 operations, even after deductions for the profit sharing distribution and income taxes, resulted in income $400,305 (GX-9). Thus, there was an increase in Cascade's 1989 capital even with profit sharing. Nonetheless, the amount was insufficient to place Cascade in capital compliance.

OTS concedes that Simpson was never ordered to refrain from making the profit sharing distribution, as originally alleged in the Notice of Charges (OTS Brief, 6, n.2). Instead, OTS now relies upon the expression of "concerns" by three directors, Blume, Woolcock and McCord (TR 99-100, 145-47, 213-14).

Messrs. Blume and Woolcock who along with Simpson made up a "Compensation Committee," testify that they expressed

serious concerns regarding any profit sharing distribution at a meeting of the Compensation Committee on December 6, 1989. However, the testimony of Blume and Woolcock is impeached somewhat by the fact that they apparently raised no protest over profit sharing at either December 12, 1989 or January 9, 1990 Board of Directors meetings and McCord was silent as well at both the December 12, 1989 and January 9, 1990 meetings. The minutes of the former state that the Compensation Committee discussed the profit sharing distribution (RX-62), and the minutes of the latter state that the profit sharing distribution was reported (RX-63). If Blume, Woolcock or McCord had serious concerns, they failed to protest at those meetings.

OTS attempts to discredit the minutes. It is true that the minutes were prepared by Simpson (OTS Brief, 14-17). However, each of the minutes was approved at the following meeting of the Board of Directors, as reflected in the minutes of the following meetings (RX-63; GX-44). Blume, Woolcock and McCord were present at the meetings, and presumably they read the minutes before voting to approve them.

Moreover, the report of the profit sharing distribution at the January 9, 1990 meeting was acknowledged by three witnesses called on behalf of Simpson, and also by two witnesses called by OTS (Rosendall, TR 244-245; McCord, TR 211, 219-220).

Incidentally, an initial OTS examination attributed the distribution of the profit

sharing to the Board of Directors, and not to Simpson individually (RX-85).

In short, the testimony of Messrs. Blume, Woolcock and McCord to some extent reflects hindsight, not exactly what they or the Board of Directors of Cascade did in 1989. Further, even after all accounting adjustments had been made and after distribution of the profit sharing, Cascade still had pretax earnings of $918,667 (GX-9), and post-tax earnings of $400,305 (As noted earlier, this addition to retained earnings was insufficient to place Cascade in capital compliance.)

In addition to Board of Directors meetings, there were other meetings which dealt with profit prospects for 1989. One of these was with Cascade auditors on December 20, 1989 where certain major

"write-downs" were discussed. The write-downs mentioned at the December 20, 1989 meeting did not entirely affect 1989 operating results, but nonetheless were items for substraction from 1989 Cascade revenue. Handwritten notes of some of those attending the meeting (Rosendall and Hogue) on December 20 (GX-45) segregate the write-downs between those affecting 1989 and those affecting other years. This is demonstrated again in the schedule attached to GX-45, which makes reference to "Adjustment to Current Year Gain" and "Adjustment to Amortization of Prior Years Gain." That schedule was not sent by the auditors until January 1990 (TR 235-36), but the substance was much the same as the oral presentation given on December 20, 1989 (GX-45 and TR 235-236). This means that Cascade's

operating income for 1989 might be adjusted only by an amount between $880,000 to $1,000,000, and the other adjustments might merely affect other years' income. There are reasons why Simpson who was at the December 20, 1989 meeting could have reached such an understanding, even if such an understanding was inaccurate under accounting standards whereby the adjustments for prior years would be taken as a substraction from 1989 income. Nevertheless, Simpson must have believed that pre-1989 deductions from income has to be taken from some account, leading to a reduction of retained earnings and a worsening of Cascade's capital insufficiency.

The notes on the meeting and the subsequent schedule are consistent with

the potential for an erroneous accounting understanding by Simpson. The information presented at the December 20, 1989 meeting (TR 235-236) refers to "current year" and "prior years" adjustments.

Non-accounting logic might be that events in 1989 would affect 1989 income, and adjustment of other years' income would be taken from non-income capital accounts. However given Cascade's capital insufficiency, such a view by Simpson must be regarded as highly self serving. It is true, however, that none of the witnesses herein expressly testify that they notified Simpson that all of the substantial adjustments explained at the December 20, 1989 meeting would be made to the 1989 income.

An OTS directive dated December 28, 1989 (included as part of GX-3 and 4) states the need for an adjustment of $1,000,000, and to "other adjustments."

Because of the key importance of this information, the OTS directive, minus the enclosure, is next reproduced per a photocopy of GX-3 [the letter is retyped below for the purposes of this Appendix B].

Office of Thrift Supervision
Department of the Treasury

Seattle District
1501 Fourth Ave. 19th Floor
Seattle, WA 98101-1693
Telephone (206) 340-2300
Fax (206) 340-2419

December 28, 1989

Mr. J. T. Simpson, President
Cascade Savings and Loan
Association
2828 Colby Avenue
Everett, Washington 98201
Docket No. 2435

Dear Mr. Simpson:

Supervisory Bulletin No. 89-16, enclosed, describes Office of Thrift Supervision policy for accounting for excess loan servicing. We believe this policy to be consistent with generally accepted accounting practices.

In a recent visit to your institution, our District Accountant, Patricia Hildebrand, noted that your method of accounting for excess loan servicing was inappropriate. A summary of her finding as is enclosed. Her review indicates "that an adjustment of approximately $1 million is necessary to correct the over valuation of approximately $3.2 million of excess loan servicing recorded since June 2, 1989.

The indicated adjustment must be recorded. In addition, please review the accounting for all other excess loan servicing at Cascade for conformance with Supervisory Bulletin No. 89-16. Please provide a written response no later than January 31, 1990, acknowledging the review and confirming that the required adjustment has been recorded. Also, please indicate the amount of any other adjustments determined to be necessary, and

the date the adjustments were made.

Sincerely,

/s/ DHT
Duane H. Thorkildsen
Senior Supervisory Agent

Enclosure

cc: Betty Reed, State of Washington

bc: FDIC
William Durbin
Ed Hedlund
Pat Hildebrand
John Potthast
Mimi Ryan
File #2 - Part II (Field Visit)
Chron File, Routing Copy

The one million amount referred to above is different from the amount set forth under the OTS column for "Adjustment to Current Year Gain" in the schedule appended to the agenda of the December 20, 1989 meeting (GX-45). As noted, the schedule was not received

until 1990, but similar figures were discussed at the 1989 meeting.

On cross-examination, witness Rosendall testifies as to his understanding of write-downs that should be attributed to the 1989 year (Rosendall, TR 253-254). The total of the write-downs Rosendall attributed to 1989 was $1,135,000. OTC correctly states that Rosendall testified to substantially larger write-downs (OTS Brief, p. 12). It is true that Rosendall testifies that only $450,000 express loan servicing income related to 1989 (Rosendall, TR 253). To that sum he adds a general loan loss reserve of $550,000, which related to loan losses which had not yet occurred. When the exact 1989 figures from Rosendall's testimony are used, and that amount is subtracted from

the projected income of $4,139,700 (RX-54), the result is a profit above target of $1,004,700. This possibly could have justified an erroneous belief by Simpson that profit sharing of some amount was warranted for 1989.

The extent of the actual write-downs, except that they were substantial, was uncertain in December 1989. The best example of this is the valuation of excess loan servicing, which the OTS estimated at $1,000,000 plus other unspecified amounts prior to June 2, 1989, (GX 3) and Peat Marwick (auditors of Cascade) estimated at $778,000 (GX-45). The fact that the regulators and the auditors had a difference of $222,000 indicates some facial uncertainty among the estimates given in December 1989 for writedowns. Simpson's views regarding

the proposed write-downs for loan servicing are set forth in his letter to Thorkildsen dated January 30, 1990 (RX-51). This letter reflecting upon Simpson's intent is attached as Appendix A. Because the amounts of the final write-downs were not exactly known in December 1989, it is incorrect to attribute total knowledge to Simpson. Such simply did not exist in December 1989 but he had ample warning that the write-down were closer to $2 million than $1 million.

OTS correctly says that profit sharing distribution could have been delayed. Of course, the distribution was made in December prior years (Simpson, TR 1039), and an audit of 1989 was not concluded until April 1990 (GX-9).

Nonetheless, there was reason for deviation from past practice particularly for Simpson himself.

The distribution of the profit sharing must be viewed in the light of contemporaneous events. Those events offer limited support for Simpson's belief that there was adequate profit to justify some profit sharing distribution for his management team even after consideration of the potential accounting write-downs effecting 1989 income. Indeed, Simpson shows that the value of the loan servicing might have been increased, rather than decreased. This is because Cascade used 3/8% for its servicing costs, in contrast to the industry standard of 1/4% (TR 1069). This resulted in a lower valuation of the asset on Cascade's books. In my opinion,

Simpson believed that if the loan servicing were to be reevaluated, then all aspects of the loan servicing should be reevaluated, which would result in an offset to the write down envisioned by Peat Marwick (Simpson, TR 1067-1070).

The profit sharing plan provided for distribution of one-half of the profits before deduction for taxes and profit sharing distribution. The projected income as of December 1989 was $4,139,700 (RX-54). After deduction of $1,000,000 pursuant to the OTS directive, the remaining profit absent write-downs for prior years and absent the creation of a loan loss reserve, was $3,139,700, which is $1,139,700 above the target. Such an imagined profit would have been in excess of the target and even could have justified profit sharing of $569,850,

which is more than the amount ($529,500) actually distributed. There was sufficient profit after deduction of $1,000,000 in accordance with the OTS directive to justify the distribution. Of course, Simpson should have been or actually was aware that other substantial write-downs were required for 1989, such as to preclude any profit sharing. As noted previously herein, his real or pretended ignorance of the magnitude of the 1989 write-downs was highly self serving.

OTS relies upon the testimony of Rosendall that Simpson advised him that the OTS directive would be ignored. However, Simpson did not ignore the OTS directive. He replied in disagreement to it on January 30, 1990 (RX-51), which is attached hereto as Appendix A. Of

course, Simpson's personal view of the correctness of the OTS directive is self-serving. He took a position to authorize profit sharing at his own risk. If he believed that there was sufficient profit after a deduction in accordance with the OTS directive, he did so on his own and not with approval of OTS.

In summary, as discussed above, according to audited financials, after deduction of all of the write-downs, Cascade had a net profit before taxes of $918,667. In order to determine the profit figure on which the profit sharing was based, it is necessary to add back both the profit sharing and the managers' bonus, in a total amount of $735,000 (RX-85). Such additions still do not meet the $2 million test level for profit sharing. Even if Simpson had doubt as to

what the final write-downs would be, he was left with less than a reasonable belief that there would be a 1989 profit sufficient to support the $529,500 distribution including the $105,000, he received. I find that his distribution to himself was in reckless disregard of his duty to Cascade and that he was unjustly enriched. As to the remaining distribution to the others, I find that Simpson reached a reasonable balance between the management needs of Cascade and its capital needs.

The 1981 Previs Loan

Simpson argues that any claim relating to the decade old Previs loan is barred by applicable statutes of limitations. OTS counters by saying that Federal statute allows a banking regulatory agency to proceed against a

former institution affiliated party if a notice of charges is served on the party within six years of his separation from the financial institution. Such test is met by OTS herein, which did not even know of the Previs matter until 1989.

Simpson, however, argues the subsection relied upon is a portion of 12 U.S.C. § 1818(i), which deals only with civil money penalties. Secondly, he says that a cause of action expired under state law cannot be revived by a Federal agency. Similarly, he says that a cause of action so expired cannot be revived by the passage of FIRREA. These contentions are dealt with supra and are rejected.

Basically, OTS asserts that Simpson knowingly caused a high risk loan by Cascade to bankrupt Previs as part of a

transaction whereby Previs bought a boat from Simpson.

The claim of OTS regarding the Previs loan is supported by the testimony of witness Graham Haight. Apart from Previs, Haight is the primary witness who testifies directly that the decision to make a loan to Previs for the ranch was influenced by Simpson's interest in selling the boat owned by Simpson to Previs.

As to Haight, there is a problem in that he testified to the contrary in a ranch foreclosure trial during 1983. At the trial, he testified that the Previs loan "definitely" should have been made, based upon the loan-to-value ratio, and that the Previs loan was the type of loans that Cascade sought, because of its high yield and loan-to-value ration

(Haight, pp. 483-486). At the prior court trial Height's testimony was inconsistent with his testimony at this administrative hearing.

OTS explains Height's prior inconsistent testimony as being only "seemingly inconsistent," for which Haight "provided a plausible explanation" (OTS Brief - 49). However, Haight gave opposite testimony under oath at two hearings. The question is at which hearing did he make a mistake. He was in my personal observation a candid witness. He also seems to have nothing to gain by his testimony before me in this OTS proceeding. I believe his present testimony, although OTS cannot "hang" Simpson solely upon the testimony of Haight. Indeed, Haight may have been just as convincing at the trial eight

years ago. His testimony, however, has other support.

OTS also connects the Previs purchase of Simpson's boat with the loan by Cascade through the testimony of Larry Carter, an attorney who represented Previs at the time and who is now a member of the firm that represents Cascade. Carter's opinion is that the boat sale and the loan are connected. This is based in part upon a statement made to him by Previs following a phone conversation by Previs with Simpson (Carter, TR 558-560). Carter was present with Previs during the conversation. He heard that portion of the conversation made by Previs (TR 558-559). After the Previs-Simpson phone conversation, Previs said to Carter, "I'm going to get the

financing but I've got to buy Mr. Simpson's boat to do that" (TR 559).

At that time Carter did not speak directly to Simpson regarding the loan or the connection between the boat sale and the loan. It is clear that Carter's initial basis for his opinion linking the boat sale to the loan was through Previs. Nonetheless, Carter testifies that he overheard Previs, as mentioned above during the telephone conversation with Simpson (Carter, TR 557-558). Carter's testimony, like the current "corrected" testimony of Haight cannot stand on its own because Carter did not hear any statement by Simpson, but it does add considerable weight to the allegations of OTS that Simpson was aware of the bankruptcy of Previs and the high risk of a Cascade loan to Previs.

The substance of the testimony of Previs is that he asked Simpson to make the loan to save the ranch and needed to buy Simpson's boat to close the deal.

Uppermost in the mind of Previs was retention of his ranch. He also was in the business of buying and selling boats. He purchased Simpson's boat for $180,000 and then resold it within six months for $360,000, realizing a profit of $55,000 after deductions for costs and improvements (Previs, pp. 377-378; 416).

Previs, in fact, used $50,000 from a subsequent refinancing of the ranch in connection with the boat. This occurred in June 1981, only two months after the initial ranch loan in April, 1981. The refinancing was hardly separate from the initial loan. Indeed Simpson obtained a benefit from the refinancing. In this

respect, $20,000 went to a boat broker for a fee Simpson otherwise would have paid and $30,000 was used by Previs to improve the boat. Simpson got his payment for the boat but Cascade was left with a bad loan for the ranch.

It is concluded that the loan to Previs was approved by officials in addition to Simpson but that Simpson was a should have been aware of the high risk of the Previs loan. The loan was exceedingly strange for Cascade which like its name did not do business east of the Cascade range of mountains where the ranch was located. Also because of the bankruptcy of Previs, the loan could not have been justified on its merits. Of course, Haight was not the only Cascade officer who approved of the loan. The Loan Committee approval form (GX-11) is

indistinct, but the refinancing was signed by at least four Cascade loan officers. The loan also was reviewed by Cascade's Board of Directors. The vote of a single member of the Loan Committee or a single director would have caused disapproval of the loan (McLaughlin, TR 304-305; Simpson, TR 964-965). Importantly, Simpson initiated the approval form for the first Previs loan. It is true that witnesses Kirkbride and McLaughlin testify that neither Simpson nor Haight applied any pressure to them (Kirkbride, TR 770; McLaughlin, TR 300; 308-309). However, it is Simpson, not other Cascade officers who are charged with responsibility herein.

The appraisals then available to loan officers show that the property had a potential value more than double the

amount of the loan (RX-3, 5, 6) but only to an outsider not someone local to eastern Washington. The financial statement of Previs available to Cascade set forth a net worth of $1,615,273 (RX-7). Certain of Previs' assets were subject to the jurisdiction of bankruptcy court. Nonetheless self serving financial statements of Previs reflected a net value of $1,615,273 after deduction for liabilities. Some of this included speculative values such as an expensive sound system and a painting of considerable importance. The loan officers of Cascade who says they were unaware of the bankruptcy of Previs might be excused, but not Simpson.

Haight was aware of the extreme financial difficulty of Previs in April or June, 1981. Haight was responsible

for the loan file and it was he who prepared the summary statements that went to the other loan officers. The credit report revealing the bankruptcy (GX-16) was received by Haight, and Carter's letter regarding Previs' bankruptcy (GX-12) was addressed to Haight. There is no mention of the bankruptcy on the loan approval forms prepared by Haight (GX-11); GX-13), which designate Previs' credit as "good" to "excellent." It is not likely that the other loan officers and the directors would have referred to Previs' credit as good or excellent if they had known of the bankruptcy. However, I neither accept nor believe the statements of Simpson that he did not know or that he had no obligation to know of the bankruptcy of Previs. Possibly, Simpson sought merely to do Previs a

favor (saving the Previs ranch and selling Previs a boat). This is speculative and not relevant. The Previs loan could not have been made without the assistance of Simpson.

Simpson embarked upon the course of helping Previs to save the ranch and to sell the boat. Simpson had an obligation to Cascade to be informed. I believe Simpson was informed but even if not, he had a duty arising out of his personal interest which he disregarded in a highly reckless manner.

He also engaged in self-dealing, at the expense of Cascade, in a manner which involves "willful disregard of his fiduciary obligation to Cascade. I find that Simpson intentionally and knowingly engaged in conduct for his own interest which directly affected Cascade's safety

and soundness by exposing it to as egregiously unsound loan. OTS is entitled to an Order of Prohibition against Simpson in addition to an order directing restitution by Simpson for the loss of Cascade from the Previs loan. That loss is $328,424 which reflects the final debt on the loan minus the final sales price of the ranch by Cascade.

Insurance Commerce, Inc. (ICI)

The third allegation against Simpson involves his control of a company that collected insurance commissions, Insurance Commerce, Inc. ("ICI"). OTS establishes that Simpson's control and operation of ICI deprived Cascade of a legitimate business opportunity which would have been a practical value to Cascade. OTS also shows that Simpson's operation of ICI, which made its money

when Cascade customers bought insurance policies with companies ICI had agreements with, amounted to a conflict of interest. Simpson seeks to justify his maintenance of ICI and receipt of benefit from its operations by reference to prior Federal banking agency policies. He shows that it would have been too expensive for Cascade to have formed a free-standing (outside of the offices of Cascade) subsidiary. He also shows that several of Cascade's Board of Directors had no interest in forming an insurance subsidiary. He also shows that an insurance agency could not have been a direct part of Cascade.

ICI made most of its money as a result of a relationship with Family Life Insurance Company ("Family Life"). ICI shared commissions with Family Life,

which received borrower lists from Cascade and then solicited these Cascade borrowers trying to sell them credit life insurance (TR 667). If Family Life sold a policy to a Cascade borrower, Cascade would collect the premiums with the borrower's mortgage payment and remit that premium to Family Life (TR 604-06; GX 48). Family Life would then in turn pay a percentage of this commission to ICI (TR 667).

GX 23 is a collection agreement between Family Life and ICI signed on behalf of ICI by Simpson. It provides that ICI shall collect the premiums due and remit them to Family Life, for which ICI will receive a portion of the commissions. According to Mr. Erickson, who was in charge of loan servicing at Cascade through the 1980's, the

collection and remission of the premiums due Family Life was done in Cascade's loan servicing division by Cascade employees (TR 604-06). Annette Hoxsey, who managed the Cascade account for Family Life through most of the 1980's, confirms that this was how the arrangement between Family Life and ICI worked (TR 662-63, 668). Ms. Hoxsey was succeeded in her responsibilities in early 1988 by Eleanor Neigel (TR 976-77). Ms. Neigel testifies that the arrangement between Family Life and ICI did not change after she replaced Ms. Hoxsey (TR 978).

GX 48 is a check from Cascade to Family Life. It evidences that Cascaded remitted the premiums due to Family Life. When a percentage of these premiums was paid back by Family Life, however, the

money went to ICI, not to an affiliate of Cascade. GX 32 through 41 are reports of miscellaneous income Family Life filed annually with the Internal Revenue Service. These reflect a total of $156,586.05 paid from Family Life to ICI from 1981 through 1990.

Ms. Hoxsey testifies that Cascade provided lists of its borrowers to Family Life (TR 667). This testimony, along with Mr. Erickson's statements concerning the remittance work done in Cascade's loan servicing department, establishes that Cascade employees performed work for ICI during their Cascade work hours. The collection agreement between Family Life and ICI specifies that ICI is responsible for the collection and remittance of premiums due Family Life (GX 23). Cascade employees also performed

functions during their time at Cascade pursuant to a relationship with another insurance company, Worthington Insurance Co., which benefitted ICI. Under the terms of that relationship, ICI received money whenever ICI "generated orders" for insurance coverage (GX 25). Fred Safstrom, Executive VicePresident at Cascade, testifies that Cascade employees referred potential customers to Worthington by directly filing referral lists (TR 766). In addition, some of the insurance orders generated from Worthington by ICI were for Cascade's own insurance needs. On such policies, Worthington and ICI would each share half the commission paid by Cascade (GX 25). Pursuant to this second arrangement, where ICI would receive half the commission Cascade paid on its own

insurance, Worthington paid ICI $4,936.56 on June 28, 1989 (GX 42).

The performance of a contractual obligation of ICI by Cascade employees on Cascade time, without compensation from ICI, is a violation of 12 C.F.R. § 563.33(b). Section 563.33(b) provides that employees of an institution shall not be permitted to work for an affiliated person unless the employee is compensated for the time by the affiliated person.

Simpson controlled ICI. By his own admission, Simpson signed corporate documents on behalf of ICI, bound ICI in contractual agreements, and negotiated loans on behalf of ICI (TR 1147-48; GX 22-23, 25, 27-31). Simpson negotiated loans ICI made to his children (TR 819, 898). In fact, Simpson testifies that he

borrowed money from ICI and negotiated those loans with himself (TR 1147-48). On one other occasion, never consummated, at least on this record, Simpson took steps to relieve his children of their debts to ICI and distribute ICI's assets (TR 1147; GX 27). As well Simpson acknowledges that he received financial benefit from his operation of ICI (TR 1156).

Thus, Simpson controlled ICI and Cascade employees performed work which resulted in material benefit to ICI. Government's Exhibit 27 is illustrative of both Simpson's control of ICI. In that letter, from Simpson to his children, Simpson writes that he is repudiating the siblings' debt to ICI and is disbursing all ICI's assets to them (GX 27). Significantly, that letter

ends: "There are extensive tax ramifications so I request you treat this mailing has highly classified material" (GX 27, emphasis in original).

His son Christopher Simpson testifies that he never received Government's Exhibit 27 from his father and never saw it prior to the investigation which preceded the filing of the Notice (TR 899). Another son, Robert Simpson, however, testifies that he had seen the letter before and thought he received it in the mail (TR 817, 823). As indicated, the debt repudiation may not have been actually consummated.

In summary, Simpson did not compensate Cascade employees for the work they performed for ICI (TR 608). Accordingly, Simpson's conduct violates 12 C.F.R. § 563.33(b). Simpson's conduct

in operating a company that made its money at the expense of Cascade is a conflict of interest and a breach of his fiduciary duty to Cascade. Additionally, Cascade could have formed a company similar to ICI. An entirely stand alone company was not necessary. Thus, Simpson's conduct amounts to a usurpation of a corporate opportunity of Cascade.

As a director of Cascade, Simpson owed Cascade a fiduciary duty of loyalty includes the duty to avoid usurpation of corporate opportunities. One who stands in a fiduciary relationship to a corporation may "not acquire, in opposition to the corporation, property in which the corporation has an interest or tangible expectancy." Id. In the Matter of O'Keefe, Director's Dec. at 23.

The seriousness with which such conduct is viewed is reflected in a FHLBB policy statement, now an OTS policy statement, noting that it is a breach of a director's or officer's fiduciary duty:

> to take advantage of a business opportunity for his own or another person's personal profit or benefit when the opportunity is within the corporate powers of the institution or a service corporation of the institution and when the opportunity is of present or potential practical advantage to the institution.

12 C.F.R. § 571,9(a).

At the hearing, Michael Scott, Program Manager of the Affiliates Policy Division in the Supervision Policy branch of OTS, appeared as an expert in the formation and operation of savings and loans subsidiaries. His branch is responsible for policy involving the regulation of subsidiaries of savings and

loans (TR 687, 698-99). The expert testimony of thrift regulators can properly establish what an unsafe or unsound banking practice. Sunshine State Bank v. FDIC, 783 F.2d at 158283, supra at 18-19.

Scott testifies that under Federal regulations, savings and loans can form subsidiaries that operate as insurance companies (TR 702). Moreover, Government's Exhibit 43, a letter from Betty Reed, the supervisor of the Washington Division of Savings and Loan Associations, states that Cascade could have formed an insurance subsidiary under State law (GX 43).

It would therefore have been permissible for Cascade to form an insurance subsidiary. Simpson insists that Cascade would have had to form a

full-fledged insurance company under applicable law and this would have been too expensive. Simpson testifies that his belief that separate facilities and employees were necessary is based on what regulators told him throughout the 1980's (TR 1141-43). Simpson points to no written statement of such requirements (TR 1143-44). Further, when asked who specifically told him these requirements, Simpson does not identify anyone (TR 1143).

ICI was only an "insurance company" in a very loose sense. In reality, ICI was only a collector of commissions shared by insurance companies.

Simpson admits that all ICI did was maintain the licenses necessary to share commissions and create the arrangements with Family Life and Worthington pursuant

to which ICI received money (TR 1154-55). Simpson states that ICI did nothing with regard to the specific policies for which it received commissions (TR 1155). ICI had no employees and no separate offices (TR 1136-37). As such, ICI was not an insurance company. It would thus have been entirely possible for Cascade to form a subsidiary which performed the same functions ICI performed.

Such an operation would have been profitable of a practical advantaged to Cascade. Scott testifies that the fees involved with securing licenses for the subsidiary and an agent would have been approximately $750 to $1000 (TR 700). Since Simpson was a licensed agent, this cost would have been less (TR 938). ICI was making an average of $16,000 a year from the commissions it received from

Family Life alone. Based on such income, Scott testifies that a subsidiary could have been profitable (TR 708).

As such, it would have been profitable for Cascade to have formed a company similar to ICI. Simpson's receipt of personal benefit as a result of this business therefore amounts to an usurpation of a corporate opportunity of Cascade. Section 571.9 of Title 12 of Code of Federal Regulations expresses OTS policy that usurpation of a corporate opportunity is an unsafe and unsound practice.

Simpson's maintenance of ICI while it benefitted from relationships with Cascade borrowers also constitute a conflict of interest.

Scott says that it is a conflict of interest for an affiliated person to

operate a company that is transacting business with the savings and loan (TR 713). The receipt of a benefit by an affiliated person as the result of insurance commissions paid by association borrowers is a conflict of interest.

Simpson states that Cascade's Board of Directors considered forming an insurance subsidiary over the years and decided not to do so. Thus, Simpson believes he was free to operate such a company himself. Such a belief is contrary to regulation. Scott testifies that even if the Board had decided not to go into the insurance business, it amounts to a conflict of interest, which is inherently unsafe and unsound for an affiliated person to form such a company on his own (TR 718-19, 72). As well, even if the Board had decided by vote or

otherwise not to form an insurance subsidiary, minutes from the Board meetings throughout the 1980's include no indication of any presentation, discussion, consensus, consideration or vote on forming an insurance subsidiary (TR 986). Simpson testifies that most items discussed in meetings were reflected in the minutes (TR 1120). The witnesses who stated they recalled discussions of insurance subsidiaries at Board meetings differ as to whether such discussions involved ICI or the details of its operations (TR 744-46, 803-05, 855-58, 891-93). One of these witnesses, Christopher Simpson, testifies that the Board voted not to form such a company. This claim is not supported by other evidence. Further, at least four Board members, two of whom have served since

1974, either recall no such discussions or had little or no knowledge of ICI and its operations (TR 106-07, 149-50, 192-93, 741).

OTHER MATTERS

The Notice in this matter does not provide for a public hearing. There were attendees at the hearing who were not witnesses. At no time did counsel for any party object to the presence of third parties. Upon my off-the-record inquiry it appears that some of the attendees were agents for the Internal Revenue Service. As well, on or about the third day of the five day hearing, there was a private discussion in which I did not participate concerning a newspaper article. Upon my inquiry, it was brought to my attention for the first time that a newspaper reporter was present during

most of the hearing. There was no motion to eject the reporter. I regret any breach of the privacy requirements of OTS. I do note, however, that any confidential information offered at the hearing related to the finances of Mr. Previs who already had been exposed to several other public proceedings. Any confidentiality that existed already had been breached by Previs himself. Further, neither Simpson, OTS, or Cascade moved to seal the record from the newspaper reporter, except in respect of one exhibit which already had been reacted.

ULTIMATE CONCLUSIONS AND FINDINGS

Based on the foregoing an Order to Cease and Desist Directing Restitution will be entered. Simpson's "free" use of Cascade employees for ICI work violated

12 C.F.R. § 563.33(b). His operation of ICI when Cascade could have benefitted from the creation and operation of such a corporation was a usurpation of corporate opportunity. Simpson was a fiduciary of Cascade while operating ICI and his conduct was also a conflict of interest and a breach of his fiduciary duty to Cascade. This was an-unsafe and practice resulting in the unjust enrichment of Simpson. Therefore, an Order to Cease and Desist directing restitution by Simpson will be entered. The requirements of § 1818(b)(6)(A) are met and Cascade is entitled to restitution from Simpson of the $161,522 ICI received as a result of Simpson's conduct. The same is true of the $105,000 received by Simpson for 1989 profit sharing and the loss to Cascade occasioned by the Previs'

loan both of which involved reckless disregard of Simpson's fiduciary duty and led to his unjust enrichment.

An order of Prohibition will be issued against Simpson based on the ICI, profit sharing and Previs transactions. Section 1818(e)(1)(A) requires a violation of regulation, an unsafe or unsound practice or a breach of fiduciary duty which standard is met here by Simpson's conduct relative to ICI, profit sharing and Previs. Section 1818(e)(1)(B) requires either a loss to Cascade or a gain to Simpson, and these occurred in every instance.

Finally, § 1818(e)(1)(C) requires that the violation, practice, or breach involve personal dishonesty or demonstrate a willful or continuing disregard for the safety and soundness of

Cascade. Simpson's realization of benefit from ICI's operation, from the Previs loan and profit sharing at the expense of Cascade amounts to self-dealing, which meets the personal dishonesty requirement. Simpson's actions in operating ICI, participating in the Previs matter and taking profit sharing were intentional actions. This meets the willful disregard standard. Further, Simpson's conduct with regard to ICI and his conduct involving the profit-sharing payments and the Previs loan, meet the continuing disregard standard of § 1818(e)(1)(C).

The standard for the Assessment of a Civil Money Penalty is also is met. Under 12 U.S.C. § 1818(i)(2)(C), such a penalty can be assessed if Simpson knowingly engaged in a regulatory

violation, an unsafe or unsound practice or knowingly breached a fiduciary duty. Simpson's conduct was committed knowingly, and it constituted an unsafe and unsound practice and a breach of his fiduciary duty to Cascade. Section 1818(i)(2)(C) also requires a showing that a party knowingly or recklessly caused substantial loss to the institution or substantial gain to the party by reason of the violation, practice or breach. Such occurred here in connection with ICI, the Previs loan and profit sharing. In further support of this decision, Appendix B which records my numbered findings of fact and conclusions of law is attached.

ORDER

Jess T. Simpson is directed to pay restitution to Cascade of $594,946 within

30 days of the effective date of this decision. Jess T. Simpson is prohibited against further participation in the affairs of Cascade or other Federally regulated banking or savings institutions. A Civil Money Penalty against the Jess T. Simpson is assessed in the amount of $138,013. The assessment should be paid within 30 days of the effective date of this decision.

By /s/ Paul S. Cross
Paul S. Cross
Administrative Law Judge, on
the 17th day of December, 1991.

APPENDIX A

CASCADE SAVINGS

January 30, 1990

Duane Thorkildsen
Assistant District Director
Office of Thrift Supervision
1501 Fourth Avenue
19th Floor
Seattle, WA 98101

Dear Mr. Thorkildsen:

In reply to your letter of December 28, 1989 concerning accounting for excess servicing, we have previously indicated to you the observation of uncertainties and differences in the elements of the calculation and the procedure to be followed.

When Ms. Hildebrand visited Cascade Savings Bank in November 1989, she expressed the newness of this issue and

it was acknowledged that reasonable uncertainty was to be expected.

Request was made that detail and specifics be provided to Cascade Savings Bank from authoritative sources at the earliest time that they were available.

Cascade Savings Bank has subsequently received detail from William Durbin on December 20, 1989, Duane Thorkildsen/Pat Hildebrand December 28, 1989, OTS, TB #43, January 26, 1990, and Peat Marwick Main on December 15, 1989 and January 11, 1990. Cascade Savings Bank analyzed the information and arrived at a tentative conclusion which was then reviewed with Peat Marwick Main and is presented herein.

It is hoped that these conclusions can be affirmed, and that we may proceed in full compliance with regulation.

Please find herewith Cascade Savings Bank's conclusions to the issue.

A brief review of Cascade Savings Bank's experience with excess servicing is appropriate.

For many years Cascade used cash basis of accounting, and accounted for interest income on mortgage loans and securities only as it was received in the form of cash payment. This was and remains the preferred basis of accounting to Cascade management.

Regulations were created making it mandatory that every savings and loan with assets over $25,000,000 go to accrual accounting.

To comply with this regulatory requirement Peat Marwick created policy and procedure for Cascade Savings.

In the implementation of the procedure Cascade chose seven (7) years as average life of a 30 year loan, an ultra-conservative election considering industry standard at the time was 12 years.

Peat Marwick strongly urged Cascade to increase projected average life of a thirty year loan from seven years to a greater number of years, and finally

after four to five years of their urging Cascade acquiesced. From 1987 to third quarter 1989 the projected average life of loans was calculated at 10 years. In the third quarter 1989, Cascade management unilaterally elected to return to a more conservative projection of eight years average life even though Peat Marwick emphasized comfort with 10 years.

It should be noted that 15 year loans parallelled the thirty year loans at Cascade wherein the projected average life was first at five years, then eight years, then six years with timing of change being the same as the thirty year loans.

It is also significant to note that Peat Marwick at first introduced the straight

line method when accrual accounting was instituted at Cascade, and subsequently a change was made for Cascade by Peat Marwick to Level Yield Method.

The academic nature of the calculation of present value of excess servicing must be clearly recognized. The calculation is significantly a prediction of future occurrences which is impossible to do with accuracy.

> It is very obvious that the speed of payoff is greater when interest rates have been high and declining, while the opposite is true when interest rates have been low and are increasing.

The semiannual and annual audits of the adequacy of the calculation used have proven adequate as it was continuously determined that the future income stream

is defined to properly amortize the amount of gain that is booked.

Quarterly updates will be made hereafter.

Over the actual life of the loans the entirety is absolutely resolved.

It is important to recognize that in the implementation of the Level Yield Method, Peat Marwick reviews average life at the time of each annual audit to determine that the projected average life has not been unduly accelerated by prepayment, and has always in the past, prior to the 1989 audit, found that the projected average lives of the entire portfolio of loans serviced was not unduly accelerated by prepayment and Cascade's projections

were conservative and well within the assumptions used by Cascade.

The procedure also had provided that Cascade check semiannually and hereafter will check quarterly to define that the assumptions have not been exceeded by prepayment.

DISCOUNT RATE

Pat Hildebrand's memo of November 20, 1989 states, (page one, paragraph four) "Excess servicing fees receivable are to be valued using a market yield . . . . The market rate for excess servicing is 13% and 15%". In communication with Peat Marwick, Cascade has learned there is a draft Thrift Bulletin superseding the December 20, 1989 Bulletin from William

Durbin. It appears the regulators are using this draft Thrift Bulletin even though it was received by Cascade on January 26, 1990. This Bulletin quotes the EITF, stipulating discount rates should be the "interest rate that a purchaser unrelated to the seller of such a financial instrument would use". A possible discount rate to use is the yield on comparable purchased mortgage servicing. Peat Marwick has advised Cascade that generic, agency servicing is yielding approximately 13% nationally. Therefore Cascade Savings Bank will use 13% for a discount rate.

Cascade's conservatism in the past and in the use of 13% at this time is further emphasized by the facts in TB #43, January 17, 1990, (page three, section

two) where it is stated, "Unacceptable rates include the teaser rate on an ARM, the institution's cost of funds, or what is sometimes called the "weighted average of new production" (weighted average teaser rates on ARMs). These rates are currently below treasury bills. . .". Cascade has consistently used discount rates in the 10% - 12½% range throughout the past several years, and has never used these unrealistic assumptions mentioned above.

These statements substantiate that discount rates should 1) be related to yields in the market place for financial instruments similar to excess servicing, 2) there are several different "acceptable discount rates", including those described above, and 3) a discount

rate is acceptable to both AP and the federal regulators when it is within a "reasonable" range of the above outlined indicators of "market yield".

Cascade Savings Bank has consistently used discount rates above those previously outlined in the GAAP literature and supervisory bulletins to calculate the value of its excess servicing.

After receiving the new data given to Cascade by Peat Marwick, at the current time, it appears that a discount rate of 13% is appropriate for calculating excess servicing.

Loan Life

Ms. Hildebrand's memo states in page one, paragraph five "A more realistic prepayment model is a 200 percent PSA model." TB #43 states (page three, section 1,C) "Institutions should use a CPR or PSA method or other methodologies that estimate prepayments over the contractual life of a loan pool sold, to calculate the excess servicing asset. The CPR or PSA assumption should incorporate current market expectations for similar loans (anticipated prepayment rates over the remaining life with limited consideration of historical experience), ...". EITF 88-11 states that prepayment rates should be those that, "market participants would use for similar financial instruments," i.e.,

mortgage backed securities. The accounting and/or regulatory literature is in contrast with Ms. Hildebrand's statement.

A 200 percent PSA model reflects an average loan life of five to six years. General industry application currently measures eight to nine years for 30 year loans. Exhibit one includes copies of the Mortgage Market Review by Prudential-Bache Capital Funding which gives actual prepayment rates, for various FHLMC coupons, (in PSA) for three months, and one year and long-term projected prepayment rates. The minimum P.S.A. during the period is 108 and the maximum P.S.A. is 200. From other data Cascade has obtained, a comparison of Prudential-Bache's prepayment rate model is within

the median of the major Wall Street firms.

Consistent with TB #43 and EITF 88-11, Cascade believes market prepayment rates should be used for estimating loan lives. However, it appears that a more sophisticated method than a simple median estimate of prepayment rates is called for.

First, new pooled MBS at Cascade consists of loans originated up to twelve months before sales. Given this, it appears a formula that takes into consideration both actual prepayments while the loans/MBS were held and the projected future prepayments would be both a more accurate method and consistant with GAAP and regulatory guidelines.

A second issue to be resolved is, which coupon of MBS to use to find the correct prepayment rate.

A range of loan coupons can be grouped into a FHLMC/FNMA MBS. Cascade has attempted to pool loans into lower MBS coupons. The major reason for this strategy is that large thrifts and mortgage bankers tend to use "current coupons", and when markets change quickly, these "current coupon" MBS tend to be adversely effected because these huge sellers are all "hitting bids" at the same time. Other institutions are operating the same way Cascade is since the remaining terms of 8½%, 8%, and 7½% FHLMC/FNMA MBS have remaining terms of 28 years and ten months. Clearly new loans are being placed into these coupons

by other institutions and those prepayment rates reflect this strategy. In an attempt to balance Cascade's method of secondary marketing against the underlying mortgage coupons, a method that takes the weighted average coupon on the MBS less 100 basis points, rounded to the nearest 50 basis point interval MBS should achieve an accurate prepayment rate reading.

EXAMPLE

October 1989 Mortgage-Backed Securities Sales.

10.15%	WAC on MBC
<1.00>	Adjustment to PC Coupon
9.15%	Use 9% PC Coupon for PSA Calculation

PSA Calculation (Data from Prudential-Bache January 19, 1990 Report)

	PSA	Weighting Factor	Total
Future Allocation	161	.66	106.26
Current Allocation	108	.34	36.72
Weighted PSA at December 31, 1989 to calculate Weighted Average Life			142.98

The Mortgage Market Review supports the conservatism of Cascade Savings Bank's assumptions of a ten year average loan life for loan originations made in the first three quarters of 1989 and an eight year average loan life for loan originations made during the last quarter of 1989.

Over the past several months long-term projected speeds have increased slightly and based on those speeds weighted average lives are in the 7.8 to 9.2 year range. The actual prepayments over the last three months have been in the 108 to 129 PSA range which would equal a 10.1 to 11 year average life. This example reinforces Cascade's conclusion that both actual and projected long-term prepayment rates must be factored in the excess

servicing calculation. PSA speeds are nowhere nearly high enough to justify new loan originations to be priced at a 200 percent speed.

As for loans originated and sold in prior years, speed data is also available. Using the same method to calculate coupons and PSA rates, seasoned loans will be adjusted as necessary to reflect new prepayment/discount rate assumptions.

Since GAAP and the regulators are now applying new methods of calculating excess servicing, Cascade will also change its methods. After communication with Peat Marwick, Cascade has recalculated the excess servicing gains booked between May 31, 1989 and October 31, 1989. The conclusion using a 13%

discount rate and market-based average life assumption is: the $3,075,000 excess servicing should be reduced to $2,551,000. Therefore a reduction of $524,000 has been made. Review of excess servicing backed in prior years and after October 1989 is continuing.

There is support in factual data that 10 year mortgage backed securities have average lives above eight to ten years at this time, the projected average lives should be nine to eleven say ten years.

There is audited data from Peat Marwick which until recently gave assurance that Cascade's conservatism was totally adequate on the excess servicing issue.

The new procedure calls for calculations to be made quarterly by Cascade Savings Bank and annually at the audit by Peat Marwick Main to ensure these criteria are within acceptable GAAP and supervisory bulletin guidelines.

Purchased Servicing Data Collection

Ms. Hildebrand states in paragraph seven, that "management does not monitor sufficient data to accurately value purchased mortgage servicing and does not track its loans by pool." Work papers prepared on a monthly basis provide balances of each purchased servicing package (pool). As with excess servicing, periodic review is made of prepayment data for any variances from past assumptions. There has been

continuous communication with Peat Marwick concerning prepayment assumptions, and at the annual audit Peat Marwick Main conducts reviews of assumptions and actual prepayments on purchased mortgage servicing.

Peat Marwick Main has given continued assurances of Cascade Savings Bank compliance at all times up to these newly originated calculations and has assured that Cascade Savings Bank has maintained adequately conservative projections of anticipated life.

Peat Marwick Main has requested that Cascade Savings Bank will define costs and other ancillary income of Loan Servicing in order to better establish values for the accrual accounting.

There are additional offsets which have not have been taken into account including ancillary revenue accounts which on an accrual basis would benefit Cascade.

It is recognized that there are various interpretations even to this time.

Much is being learned.

Standards are being evolved.

It is necessary to emphasize awareness that projections deal with the unknown future with many unknown variables.

Cascade Savings Bank has held a conservative course in order to be within compliance.

The conservatism has served reasonably well.

Cascade Savings Bank has committed continued compliance at all times within reasonable ability to do so.

Peat Marwick Main has reaffirmed Cascade's calculations and compliance in their audits through 1988.

It is consistent with Cascade Savings Bank Policy and Procedure that if at any time accelerated prepayment greater than projections is experienced, then proper

adjustments to excess servicing will be made no less frequently than at quarterly periods.

Yours very truly,

CASCADE SAVINGS BANK

/s/ J.T. Simpson
J. T. Simpson
President and Chairman

PC: Bill Durbin
Betty Reed
Pat Hildebrand
Viktar Rzeteljski
Bert Houge
Board of Directors
Executive Committee

APPENDIX B*/

FINDINGS OF FACT

A. JURISDICTION

1. Cascade is a state-chartered mutual savings and loan association maintaining its principal place of business in Everett, Washington.

2. Cascade is a "savings association" as defined by Section 2(4) of the Home Owners Loan Act ("HOLA"), as

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*/ This appendix is coordinated with the text of the main body of this decision. It is composed in major part from the proposed findings of fact and conclusions of law of the parties. Such proposed findings are submitted by the parties in the expectation that they will be adopted. It would be wasteful to rewrite them for the mere sake of appearance. The exact process followed herein has been use the word processing diskettes of the parties which are computerized copies of the hard copy (paper) submissions of the parties. Hundred of changes, deletions, modifications and additions have been made. The findings and conclusions are entirely my own.

amended by Section 301 of the Financial Institutions Reform, Recovery and Enforcement Act ("FIRREA"), 12 U.S.C. § 1462(4), and Section 3(b) of the Federal Deposit Insurance Act ("FDIA"), as amended by Section 204 of FIRREA, 12 U.S.C. § 1813(b), and is an "insured depository institution" as defined by Section 3(c)(2) of the FDIA, as amended by Section 204 of FIRREA, 12 U.S.C. § 1813(c)(2).

3. Until August 9, 1989, the accounts of Cascade were insured by the Federal Savings and Loan Insurance Corporation ("FSLIC") pursuant to Section 403(b) of the National Housing Act ("NHA"), 12 U.S.C. § 1726(b), by reason of which it was an "insured institution" within the meaning of the NHA.

4. As of August 9, 1989, pursuant to the provisions of FIRREA the insurance of the accounts of Cascade was transferred to the Federal Deposit Insurance Corporation.

5. Until August 9, 1989, the Federal Home Loan Bank Board ("Bank Board"), as operating head of the FSLIC, was the regulatory agency with jurisdiction over Cascade and its officials pursuant to Sections 403 and 407 of the NHA, 12 U.S.C. § 1726 and 1730.

6. As of August 9, 1989, pursuant to Section 3(q) of the FDIA, as amended by Section 204 of the FIRREA, 12 U.S.C. § 1813(q), the Office of Thrift Supervision ("OTS") succeeded to the interests of the FSLIC with respect to the supervision and regulation of all

savings associations, and thus became the "appropriate Federal banking agency" with jurisdiction over Cascade and persons participating in the conduct of the affairs thereof.

7. The Director of OTS has the authority to institute administrative proceedings to determine whether a cease and desist order directing restitution and other affirmative corrective relief, prohibition order and order assessing a civil money penalty should issue against Simpson pursuant to Section 5(d)(1)(A) of the HOLA, as amended by Section 301 of the FIRREA, 12 U.S.C. § 1464(d)(1)(A), and Section 9 of the FDIA, as amended by the FIRREA, 12 U.S.C. § 1818.

8. At all times relevant herein, Simpson was President and Chairman of Cascade's Board of Directors. As such,

he was an officer, director and person participating in the conduct of the affairs of Cascade and, as such, was an "institution-affiliated party" of Cascade as that term is defined by section 3(u) of the FDIA, as amended by Section 204 of the FIRREA, 12 U.S.C. § 1818(u). By virtue of these positions, Simpson is subject to the OTS's authority to maintain cease and desist and prohibition proceedings, including restitution, and to assess civil money penalties.

9. Simpson resigned as an officer and director of Cascade on March 13, 1990 (TR 916).

10. The Notice of Charges was by the Office of Thrift Supervision ("OTS") on February 12, 1991.

11. Cascade has not been placed into conservatorship or receivership with

OTS or any other federal or State of Washington banking regulatory authority (TR 51). Cascade is solvent, with a stated equity of $8,616,692 as of December 31, 1989 (GX-9). Cascade's true value is substantially higher (TR 927-928).

12. Cascade is not a party to the Notice of Charges filed by the OTS herein.

13. Cascade hired K.P. Zech of Z-Associates, Inc. to conduct an investigation, which was concluded in June 1990 (the "Zech Report"). The Zech Report contained certain allegations against Simpson (RX-83).

14. At all relevant times, Cascade was represented by its attorneys, Preston Thorgrimson Shidler Gates & Ellis ("Preston"). Preston prepared a draft

complaint, based upon and incorporating the allegations contained in the Zech Report (RX-83).

15. Cascade made an informal claim to Simpson. Cascade and Simpson entered into settlement discussions, but no settlement was reached (RX-83).

16. Preston assisted OTS in its investigation of these matters, including indirectly the interrogation of witnesses and the production of documents (RX-83).

17. The Notice of Charges include and are based in part on the allegations contained in the Zech Report and in the draft complaint prepared by Preston (RX-83).

18. Cascade has not assigned its claims against Simpson to OTS or entered into any similar agreement with OTS (TR-51-55). OTS has stated that any

recovery made from Simpson in this matter will be delivered to Cascade (TR 51-55).

B. PROFIT SHARING DISTRIBUTION

19. In 1989 and in previous years, Cascade had a profit sharing plan ("Plan"). Under the Plan, Cascade's Board of Directors selected a target for Cascade's net profit before deductions or taxes, profit sharing distribution and managers bonus ("Target"). The Target was selected at the beginning of each calendar year. Half of all profits above the Target were available for distribution under the Plan (TR 93).

20. Each year, the distribution under the Plan was made at year-end based upon profit projections then available (TR 1039).

21. The Target for 1989 was $2 million (TR 93).

22. The participants in the Plan were managers and officers of Cascade (TR 93).

23. The purpose of the Plan was to provide motivation for Cascade's managers and to reward them for their performance as employees (6x8 and TR 1037-38).

24. In January 1989, Cascade's managers were advised of the Target. Periodically during 1989 Cascade's managers were advised of the profits and potential profit sharing distributions (TR 1040-1043; RX-66, 71).

25. Cascade's managers developed expectations of receiving substantial profit sharing distributions at the end of 1989 (TR 1046-1047).

26. Cascade's profit projection available in December 1989 was dated December 12, 1989 (RX-54). The

projection showed a net profit of $4,139,700 before taxes and profit sharing and managers bonus distributions. Under the terms of the Plan, $1,069,850 was available for distribution.

27. FIRREA became effective in August 1989. FIRREA contained new capital requirements. Cascade met the tangible and core capital requirements, but did not meet the risk-based capital requirement (TR 55).

28. On October 16, 1989, OTS notified Cascade by letter that it would fail to meet new capital requirements imposed by FIRREA (GX 5; TR 27-28). This letter notified Cascade that it was required to increase capital ratios significantly (GX 5).

29. On November 9, 1989, OTS notified Cascade by letter that the new

capital requirements were to go into effect on December 7, 1989 and that Cascade would fail one of more of these new capital requirements (GX 6).

30. On November 14, 1989 members of OTS met with the Cascade Board of Directors and senior management. Among those attending the meeting on behalf of OTS were Duane H. Thorkildson and Bill Durbin. Betty Reed, Washington State Supervisor, also attended the meeting. FIRREA and Cascade's compliance with FIRREA were discussed at the meeting (TR 61-62; GX-7; RX-76).

31. At this meeting, which Simpson attended as Chairman of the Board, the OTS representatives discussed Cascade's failure to meet the capital requirements and the need for restricted growth and

new capital with Cascade's Board of Directors (GX 7; TR 29-31).

32. Based on the paragraphs above, by November 11, 1989, Simpson knew that Cascade failed one requirement for regulatory capital and that Cascade needed to generate new capital (GX 5-7).

33. Cascade currently has an approved capital plan (TR 68).

34. Distributions under the Plan were to be based on Cascade's 1989 income. Compliance or lack of compliance with FIRREA's capital requirements did not effect the 1989 income (TR 216, 517-518, 1049-1050).

35. Distributions under the Plan are determined by a Board of Directors Compensation Committee ("Committee"). In 1989, the Committee was composed of

directors Bruce Blume, Patrick Woolcock and Simpson (TR 91; 142).

36. The Committee met on December 6, 1989 at the Seattle Golf Club in Seattle, Washington (TR 98).

37. At this meeting, the Committee discussed distributions to be made under the Plan and the impact of FIRREA (TR 98-100).

38. Blume and Woolcock expressed concern at this meeting regarding Cascade's compliance with the capital requirements of FIRREA, but they did not direct Simpson not to distribute the profit sharing (TR 119; 163).

39. On November 20, 1989, Patricia Hildebrand, OTS District Accountant in Seattle, determined after review that Cascade had overvalued its excess loan servicing fees asset, the amount of money

Cascade would receive for servicing loans over their future estimated life, by approximately $1 million (GX 4; TR 76). In a conversation on November 22, 1989, Ms. Hildebrand told Simpson of this conclusion (TR 77-79).

40. A regularly scheduled Cascade Board of Directors meeting was held on December 12, 1989. The Committee reported the scheduled profit sharing distributions, and discussed the magnitude of the proposed distributions (TR 807, 863, 1057). The minutes of the meeting stated:

> Compensation for year end [sic] 1989 including Managers Bonus and Profit Sharing in compliance with budget '89 was reviewed. Report of the Directors Compensation Committee meeting covered the scheduled payments, and the projected compensation adjustments for 1990 (RX-62).

41. The minutes of the December 12, 1989 Board of Directors meeting were approved at the next regularly scheduled Board of Directors meeting, held n January 9, 1990. (RS-63)

42. On December 15, 1989, Viktor Rzeteljski, the engagement partner for KPMG Peat Marwick ("Peat"), Cascade's auditors, wrote Simpson informing him of Peat's opinion that Cascade had overvalued its excess loan servicing fees asset (GX 46).

43. On December 20, 1989, a meeting was held between Peat Marwick and certain Cascade directors and managing personnel. The subject of the meeting was certain potential adjustments to Cascade's financial statements, including those matters set forth in the agenda to the meeting (GX-45). This was the first

occasion at which significant potential adjustments to income were discussed at the Director level.

44. At this meeting, Peat Marwick advised Cascade directors and managing personnel of a potential adjustment for "Gain on loan sale calculations" in the amount of approximately $780,000 for 1989. Peat Marwick also discussed other adjustments, which were not expressly designated as being related to 1989 income (TR 499-504).

45. Mr. Rzeteljski also reported that Cascade had overvalued this asset by $1.7 million for prior years, for a total proposed reduction in value of nearly $2.5 million (GX 45; TR 501-02).

46. At this meeting, Peat Marwick described the results of analyses of gain on loan sale calculations conducted by

Peat Marwick, by OTS and by Cascade. The description, as later somewhat differently confirmed in writing is broken down into categories of "Adjustment to Current Year Gain" and "Adjustment to Amortization of Prior Years Gain." The calculation of the adjustment for the current year gain by OTS was $1,000,000 and the calculation for the adjustment to current year gain by Peat Marwick was $778,000 (GX-45).

47. During the December 20, 1989 meeting, Peat also reported its conclusions that the value of other assets should be reduced. Although specific numbers were not discussed, Mr. Rzeteljski stated at this meeting that these writedowns would be substantial (TR 501, 504, 542-43).

48. A possible but not reasonable inference to be drawn from the statements of Peat Marwick and from the schedule distributed at this meeting was that Cascade's 1989 income should be adjusted by a reduction of approximately $800,000 to $1,000,000 as a result of recalculation of gain on loan sales for 1989, and that other reductions for prior years were likely.

49. A possible but not reasonable inference to be drawn from the comments of Peat Marwick and from the description at this meeting might have been that additional adjustments would be made to Cascade's financial statements for periods other than 1989.

50. Frank McCord, a member of Cascade's Board of Directors who attended the December 20, 1989 meeting, told

Simpson in a private conversation at the December 20, 1989 meeting that if Cascade would not have profits for 1989, payments under the Plan should not be made (TR 213-14).

51. Simpson was aware that Peat's recommendations at the December 20, 1989 meeting would result in reduced profits for Cascade and that reduced profits would directly affect whether the target would be met and payments made under the Plan in 1989. He (Simpson) believed that the accounting was esoteric and needed more study (TR 509 as per OTS witness Rzeteljski). ("These were esoteric kinds of accounting methodologies" as stated by Simpson to Rzeteljski - TR 509.)

52. Because of his doubts about the new accounting concept, Simpson stated his intention at the December 20, 1989

meeting to distribute payments under the Plan but did not indicate the amount of such disbursement (TR 509).

53. On December 28, 1989 OTS issued a directive ("OTS directive") to Cascade to record an adjustment of $1 million (GX-3). OTS gave Cascade no other directive regarding the 1989 income.

54. It is not clear when the OTS directive was received by Cascade. On brief, both OTS and Respondent say it was received on December 29, 1989, the last business day of 1989 and the day on which the profit sharing distributions were made (GX-3; TR 278). Receipt of the OTS directive by Cascade on December 29, 1989 appears unlikely, but I accept the separate statements of counsel that the date of receipt of the OTS directive by Cascade was 12-29-89. I note, however,

that Simpson says that he could not have seen it on that date while witness Rosendall says Simpson saw it that day.

55. In the past, Peat had recommended that Cascade create a general loan loss reserve, but Cascade had not created such a reserve by year-end 1989. Peat believed it a more prudent business practice to create general reserves rather than waiting until a particular loan deteriorated to the point where a specific reserve needed to be created (TR 233-24, 503-04; 540).

56. Regulations require that if an institution has classified assets, assets determined to be substandard or doubtful, it must create a general loan loss reserve. 12 C.F.R. § 563.160(d).

57. Cascade had classified assets and, as such, was required by regulation

to create a general loan loss reserve (TR 234).

58. The projected net income for 1989, before deduction for taxes and distribution of profit sharing and managers bonus, was $4,139,700 (RX-54). After deduction of $1,000,000 pursuant to the OTS directive, the projected net income before deduction for taxes and distribution of profit sharing and managers bonus was $3,139,700. Under this scenario, one which did not actually exist, net profit sharing in excess of the Target of $2,000,000 was $1,139,700. The amount available for distribution pursuant to the Plan then would have been one-half of this amount, which is $569,850. However, such a calculation is false because it fails to take into account the need for a loan loss reserves

and certain additional adjustments which were discussed on December 20, 1939 with Simpson.

59. Some of the adjustments discussed at the December 20, 1989 meeting were based upon changes in accounting and regulatory standards (TR 513-514). The calculation of the adjustments were complex and were based upon estimates of several variables (TR 80-86). However, creation of a general loan loss reserve was not complex and should have accomplished in 1989 or earlier.

60. Simpson questioned whether the proposed adjustments were appropriate (TR 1086; RX-51).

61. Determination of the final adjustments to the 1989 income and the final audit of the 1989 income were not

concluded until several months after the profit sharing distributions were made (GX-9).

62. Profit sharing distributions in the amount of $529,500 were made on December 29, 1989 to various managers of Cascade upon the direction of Simpson (GX-8 and TR 277-78, 285-86).

63. Included in the profit sharing distribution was a deposit of $105,000 into the deferred compensation account maintained by Cascade for the benefit of Simpson (GX-8 and TR 1129).

64. The distribution of the profit sharing was reported to the Cascade Board of Directors and approved by the Cascade Board of Directors at the next regularly scheduled meeting, held on January 9, 1990 (RX-63; TR-211, 219-220, 244-245, 808, 814-805, 1082-1083).

65. OTS and State of Washington examiners conducted an examination of Cascade, commencing in January 1990. That examination attributed the decision to distribute the profit sharing to the Board of Directors and not to Simpson personally (RX-85).

66. Cascade was an operating entity, and the expectations and morale of its managers could not be ignored in determining the amount of profit sharing to be distributed.

67. Cascade was required to exercise its best business judgment in making the profit sharing distribution, in consideration of its obligations to its managers pursuant to the Plan, the need to maintain the morale and continued employment of the recipients of the profit sharing, the projected income, the

OTS directive, and the advice of Peat Marwick.

68. Simpson and Cascade eventually complied with the OTS directive.

69. Simpson was not directed to halt the profit sharing distribution.

70. The final 1989 audit, a report of which was transmitted by Peat to Cascade in April, 1990, included writedowns of $1.25 million for excess loan servicing; $135,000 for loan origination fees; $125,000 for purchases servicing; and the creation of $325,000 in specific loan loss reserves and $550,000 in general loan loss reserves (GX 9; TR 238).

71. The 1989 audit reflected a NPBT for Cascade of $918,667 (GX 9).

72. Even if the $529,500 paid out under the Plan is added to the NPBT, the

$2 million would not have been met, and no payments could have been distributed under the Plan (TR 546).

73. Given Cascade's inadequate capital, all profits should have been contributed to retained earnings or capital.

74. If Simpson had waited until Cascade's 1989 audit had been completed pursuant to the concern expressed by compensation committee members Blume and Woolcock, no payments would have been made under the Plan.

75. Cascade did not experience a net loss during 1989 by virtue of the distribution of the profit sharing, although capital would have been increased substantially had that distribution not occurred, and capital insufficiency would have been lessened.

C. THE PREVIS LOAN

76. In 1975, Randy Previs purchased the Valley View Ranch (the "Ranch"), a 66-acre parcel of land located in Thorp, Washington (TR 344-45).

77. Mr. Previs lived on the Ranch until he sold it in 1978 (TR 345). He then pledged the contract from this sale as security for a loan he received from Paul Deyong (TR 346). The purchaser of the Ranch defaulted, and Deyong foreclosed on the contract (TR 346).

78. Mr. Previs filed for bankruptcy in February, 1980 (TR 346).

79. The Ranch became part of the bankruptcy estate, but the bankruptcy trustee elected not to pursue the Ranch as an asset for the benefit of Mr. Previs's creditors and abandoned the property to Deyong (TR 346-47).

80. Deyong then attempted to sell the Ranch. Mr. Previs had an agreement with Deyong whereby Mr. Previs was given an opportunity to match any offer Deyong received on the property (TR 347-48).

81. In early 1981, Randy Previs attempted to obtain financing to match an offer of $250,000 Deyong had received and buy back the Ranch (TR 348-49).

82. Mr. Previs's application for financing to buy back the Ranch was rejected by 20 to 30 lenders (TR 349-50). These lenders rejected Mr. Previs's application based, in part, on Mr. Previs's outstanding bankruptcy (TR 350).

83. As a business venture, Mr. Previs occasionally bought large pleasure boats, refurbished them, and resold them at a profit (TR 351-52).

84. James McGinnis, a yacht-broker with McGinnis Yacht Sales assertedly suggested to Mr. Previs that Simpson might provide financing for the Ranch if Mr. Previs bought a boat, the Laelanne, owned by Simpson (TR 352). (McGinnis was not called as a witness.)

85. Mr. Previs then contacted Simpson directly, and Previs says that Simpson told him Cascade would finance the purchase of the Ranch if Mr. Previs bought the Laelanne (TR 354-55, 361-64).

86. In one of their first conversations, Mr. Previs assertedly told Simpson of the bankruptcy proceeding (TR 355-56).

87. Within hours of reaching a satisfactory oral agreement regarding the sale of the boat, Previs inquired of Simpson regarding a possible loan from

Cascade (TR 1015-1016). Simpson referred Previs to Cascade's Seattle branch (TR 1017-1018).

88. Previs then applied for a loan to Glen Kirkbride ("Kirkbride"), the manager of Cascade's Seattle branch (TR 356-357). The purpose of the loan was purchase of the real property located at Thorp (The Valley View Ranch "Property" or "Ranch).

89. In support of his loan application Previs submitted to Cascade an appraisal by Western Appraisal Company, M.A.I. appraisers, dated April 23, 1981 showing the value of Property as $627,000 (RX-5 and 6), and an evaluation by Murray Realty & Investment dated April 20, 1981 showing the market value of the Property as between $650,000 to $670,000 (RX-3 and 4).

90. In support of his loan application, Previs submitted to Cascade financial statements snowing his net worth of $1,615,273 as of March 10, 1981 (RX-7).

91. In support of his loan application, Previs submitted Cascade a letter of recommendation from Larry Carter ("Carter"), an attorney then representing Previs (RX-10). Carter is a partner in the law firm which is currently general counsel to Cascade (TR 563-564)

92. In its underwriting of the loan application by Previs, Cascade loan personnel obtained at least two credit reports on Previs (RX-2; GX-10).

93. Previs was personally in bankruptcy proceedings at the time of his application to Cascade. The record does

not exactly indicate whether this fact was known to all key Cascade loan personnel prior to the granting of the loan.

94. Simpson asked Graham Haight, Senior Vice-President of Cascade's loan division, to organize Mr. Previs's loan application and bring it forward (TR 448).

95. The fact of a prior Previs' bankruptcy filing was disclosed on the original loan application he submitted for the mortgage loan dated April 27, 1981 (GX 10). The Previs statement was in terms of the "last seven years."

96. During his review of Mr. Previs's loan application, Mr. Haight reviewed a credit report which noted Mr. Previs's outstanding bankruptcy, an adverse judgment for $60,000 and other

items of derogatory credit (TR 449, 451-52; GX 16).

97. The Ranch was outside Cascade's lending area; Cascade had never loaned money on real estate east of the Cascade mountains (TR 324-25, 453, 460-61, 791-92).

98. Cascade rarely loaned money on rural, non-owner occupied property, and when it did, it preferred that the property produce income (TR 456-57, 329).

99. Cascade did not normally lend money to borrowers with outstanding bankruptcies (TR 329, 454).

100. After his review, Mr. Haight concluded that Cascade should not make the loan to Mr. Previs (TR 452, 454, 473).

101. When Mr. Haight assertedly informed Simpson of his conclusion that

Cascade should not loan money to Mr. Previs, Simpson responded that Cascade would approve this loan notwithstanding Mr. Height's conclusion (TR 454-55, 473).

102. Mr. Haight had a short period of days to close this loan (TR 449, 474).

103. On or about April 27, 1981, Cascade's loan committee approved a loan to Previs' nominee, the Katie Previs Land Company, in the amount of $258,000. The loan committee approval form was initialed by Haight, Cote and Simpson (GX-11, GX 17 and TR 458). The loan was secured by a deed of trust on the Property. The Property had a potential value more than double the amount of the loan.

104. On April 27, 1981, the Katie Previs Land Co., with Randy and Katie Previs signing as principals, borrowed

$258,000 from Cascade in order to purchase the Ranch. In return for this loan, Cascade took a note secured by the Ranch, due in 90 days and bearing a 2% loan fee and a 17% interest rate (GX 11, 17).

105. Graham Haight testifies that he was pressured by Simpson to approve the Previs loan. Height's testimony is somewhat impeached by his prior inconsistent testimony at a foreclosure trial in 1983 and standing alone is not entirely credible (TR 483-486; 488-489). However, Height's testimony has other support.

106. Previs' credit at the time of the granting of the loan was rated as "good" by Cascade (GX-11). Other than Haight, none of the loan officers who approved the loan testify that they had

been contacted by Simpson or pressured by Simpson in any fashion.

Kirkbride says he was never pressured by Simpson to approve the loan (TR 770).

107. OTS has offered no independent expert testimony that the loan was not properly underwritten or should not have been made.

108. Simpson was the originator of many loans, which he routinely referred to various Cascade loan officers. It was the practice at Cascade to underwrite loans referred by Simpson in the same fashion as all other loans (TR 299-300; 770; 990-991).

109. It would have been reasonable for Simpson not to advise members of the Cascade loan committee of the sale of his boat to Previs out of concern that it

might influence their underwriting of the Loan. However, it was not reasonable for Simpson to avoid knowledge of adverse information concerning the loan.

110. In addition to the testimony of Haight and Previs, Simpson is connected to the underwriting and decision to make the loan to Previs by his original referral of Previs to Kirkbride and his initialing of the loan approval form (TR 1019; 1021-1022). Simpson also is implicated upon the testimony of Carter.

111. On April 28, 1981, Larry Carter, Mr. Previs's attorney in the bankruptcy proceeding, wrote Cascade concerning Mr. Previs's loan application. The April 28, 1981 letter specifically refers to Mr. Previs's outstanding bankruptcy (RX 10).

112. Mr. Carter's April 28, 1981 letter also refers to a financial statement filed by Mr. Previs with the loan application, which lists the Previs's net worth as $1,615,273 (RX 10, 7).

113. Mr. Carter's April 28, 1981 letter states that approximately $1,520,000 of the Previs's assets listed on Respondent's Exhibit 7 is under the jurisdiction of the bankruptcy court (RX 10, 7).

114. On or about June 3, 1981 Previs obtained a reduction in the purchase price of Simpson's boat from $200,000 to $180,000. He also obtained a change from a cash payment to a promissory note, secured by the boat and certain real property, not the Ranch (TR 1024-1026).

115. On June 12, 1989 Previs (Simpson says for the first time) advised Simpson of his intention to borrow an additional $50,000 from Cascade, with $20,000 of the proceeds of the loan to be used to pay a commission to a boat broker in connection with the purchase of the boat and with $30,000 of the proceeds to be used to make improvements to the boat (GX-15).

116. Also, on June 12, 1981, Jess T. Simpson net with Randy Previs and Larry Carter, Previs's attorney, to discuss the purchase of Mr. Simpson's yacht by Mr. Previs (GX 15).

117. As a result of the meeting referred to immediately above, Previs applied to have the note referred to in paragraph 63, above, increased to $310,000. Of this money, approximately

$260,000 was to pay off the existing note, and as mentioned $20,000 was to pay a boat broker for his commission on the sale of the yacht, and $30,000 was to be used for repairs on the yacht (GX 15).

118. Simpson says that he was not aware of Previs' intention to borrow additional funds from Cascade in connection with the boat until he was so informed by Previs on June 12, 1981, approximately six weeks after Previs had obtained a loan from Cascade for the purchase of the Ranch (TR 1027-1030).

119. Prior to the approval of the original mortgage loan on April 27, 1981, Previs says that he and Simpson had agreed that Previs would refinance the mortgage loan at a later date, to pay for repairs to the yacht (TR 335, 360-61,

363). Simpson disputes this, as noted above.

120. On June 19, 1981, Cascade granted a second loan of $323,000 to the Katie Previs Land Co. in order to pay off the existing note. In return, Cascade took a new note secured by the Ranch which was due in 90 days and bore a 2% loan fee and a 19.5% interest rate (GX 13, 17). Also, $50,000 of the proceeds of the second loan was used for the boat; $30,000 for improvements and $20,000 for the Commission.

121. The refinancing referred to in paragraph 70, above, was approved on June 18, 1981 by Cascade's Management Loan Committee; specifically, the loan committee approval form was initialed by Haight, Totten, McLaughlin and Hamanishi (GX 13).

122. None of the proceeds from either loan to Previs was received by Simpson, although Simpson was paid for the boat and was spared the payment of a Commission of $20,000 (TR 1028).

123. Carter assisted Previs in obtaining the loan from Cascade and assisted Previs in his purchase of the boat from Simpson. Carter did not believe that Previs' purchase of the boat from Simpson constituted a bribe (TR 573).

124. On July 1, 1981, when the Previs Equipment Co., with Randy and Katie Previs signing as principals, finally contracted to purchase the yacht from Jess T. Simpson for $180,000, the contract called for $80,000 to be paid by October 15, 1981; $50,000 was to be paid on October 15, 1982; and $50,000 on

October 15, 1983. The interest rate varied from 12 to 15 percent (GX 14).

125. On April 20, 1962, Cascade granted an additional loan of $399,500 to the Katie Previs Land Co., in order to pay off the existing note. In return, Cascade took a new note secured by the Ranch, due in 90 days and bearing a 2% loan fee and a 21% interest rate (GX 17). Immediately, before foreclosure, the debt reached $538,424, through compounding of interest and loan fees.

126. According to Simpson, Previs' purchase of Simpson's boat was independent of and not related to the loan he obtained from Cascade in April 1981 in the amount of $250,000 in connection with the Ranch.

127. The fair market value of the boat at the time of the sale was equal or

in excess of $180,000, as evidenced by the fact that Previs resold the boat for $360,000 within six months, earning a profit of $55,000 after deduction for costs and improvements much of which was done Mr. and Mrs. Previs (TR 1033; 377-378; 416). At that time, Simpson was paid for the boat by Previs.

128. On January 25, 1983 Cascade filed a lawsuit to foreclose on the Previs loan, which was then in default (RX-16).

129. On March 2, 1983 Previs filed a pleading entitled Answer, Affirmative Defenses, Counterclaim and Third Party Complaint in the foreclosure lawsuit (RX-17). In that pleading, Previs disclosed the facts relating to the purchase of the boat from Simpson.

130. A trial on Cascade's complaint was held in Kittitas County, Washington. The trail was concluded in December 1983. The court entered judgment in favor of Cascade. As a result, Cascade obtained title to the Property (TR 1032).

131. Relevant facts regarding Previs' purchase of Simpson's boat and the use of $50,000 from the first refinancing of the loan in connection with the boat were disclosed during discovery and the foreclosure trial (TR 403; 486; 623-624; 1032). Cascade was represented during the discovery and at the trial by its attorney, William F. Almon, as well as various bank employees (TR 1032).

132. On August 5, 1985 Cascade entered into a contract to sell the Valley View Ranch to Dr. and Mrs. Larry

Bundy. The purchase price was $350,000 (RX-11).

133. In connection with his contract to purchase the Valley View Ranch from Cascade, Bundy paid $10,000 to Cascade as a down payment and $10,000 as a loan extension fee. The sale to Bundy was not consummated, and Cascade retained ownership of the Valley View Ranch (RX-11).

134. In September 1988, Cascade sold the Valley View Ranch to Mr. and Mrs. James Ogden at the price of $210,000 (GX-21).

135. Although Cascade's Board of Directors approved the loans to Mr. Previs, such approval occurred without sufficient Board knowledge that Jess T. Simpson was negotiating the sale of his yacht to Mr. Previs, that Mr. Previs had

an outstanding bankruptcy, that the loan was approved in a much shorter time period that usual for mortgage applications, and that Mr. Previs had no steady source of income with which to repay the loan (TR 153-54, 471). The debt of Previs at the time of foreclosure was $538,4243. Of this amount Cascade recovered $210,000 upon sale of the Ranch. The difference is $328,424 which is the amount of restitution presently sought by OTS from Simpson for the Previs loan, while this total includes fees and penalties, the amount reflects Cascade's loss of opportunity to use the loan amount elsewhere for profit making.

D. INSURANCE COMMERCE, INC.

136. Insurance Commerce, Inc. ("ICI") is a corporation which was owned by Simpson or members of Simpson's family

prior to the time Simpson became affiliated with Cascade in 1955 (TR 918; 935-936).

137. In 1975 Simpson transferred all of his ownership interest in ICI to his adult daughter, who lived in Hawaii (RX-27; TR 940-942).

138. After the transfer of the ownership of ICI to his daughter in 1975, Simpson continued to be involved in the affairs of ICI.

139. ICI was licensed as an insurance agent under the laws of the State of Washington. ICI received commissions from various sources from the sale of insurance policies (TR 938).

140. The existence of ICI, its ownership by the Simpson family, and its collection of commissions was commonly

known throughout Cascade (TR 158-159, 205, 315-317, 620-621, 764, 839).

141. At all relevant times herein, it has been illegal for Cascade to engage directly in the insurance industry. At some time, it became legal for Cascade to establish a subsidiary to engage in the insurance industry (GX-43; TR 943-944).

142. During the 1980's Cascade had at least four separate subsidiary corporations. Each one of them resulted in losses to Cascade, and ultimately Cascade closed or sold each subsidiary (TR 945-946).

143. On several occasions during the 1980's, several members of Cascade's Board of Directors considered whether it should establish an insurance subsidiary. On no occasion did the Board of Directors elect to establish a subsidiary to engage

in the insurance industry and there never was a formal vote (TR 108, 742, 803-805, 841, 855-857, 957-958).

144. Various members of Cascade's Board of Directors were inclined against engaging in the insurance industry because of its unprofitable experiences with other subsidiaries and its concern that the establishment of a subsidiary to do that which Cascade could not do directly constituted a circumvention of the law (TR 840, 743-744, 1012-1013).

145. Nonetheless, it appears that Cascade and ICI were one and the same. From January 1, 1981 until at least March, 1990, Simpson negotiated loans made by ICI, including at least one made to himself, signed corporate and official documents on behalf of ICI, and attempted on at least one occasion to disburse its

assets (GX 22-23, 25, 27-31; TR 819, 898, 1147-48).

146. For the period from 1981 until at least March, 1990, ICI received at least $156,486 total income from Family Life Insurance Company ("Family Life"), credit life insurance company in Seattle, Washington (GX 32-41).

147. From January, 1981 until at least March, 1990, Family Life paid these moneys to ICI in return for services performed by Cascade employees (TR 604-06, 662-63, 667-68).

148. Specifically, from January 1, 1981 until at least March, 1990, Cascade provided Family Life with lists of Cascade mortgage borrowers; Family Life would then solicit these Cascade borrowers in an attempt to sell them a mortgage life insurance policy. Once

such a policy was sold, Cascade collected the insurance premium payments with the monthly mortgage payments and remitted the premium payments to Family Life. For this service of Cascade employees, ICI received a payment from Family Life based on a percentage of the premium payments remitted to Family Life by Cascade (TR 604-06, 662-63, 667-68; GX 23).

149. ICI's contractual arrangement with Family Life provided that ICI would perform the collection and remittance functions detailed in paragraph 88, above, which were actually performed by Cascade employees (GX 23).

150. Neither ICI nor Simpson compensated Cascade employees for the work they performed during business hours at Cascade which benefitted ICI and Simpson (TR 608).

151. Simpson concedes he derived personal financial benefit from the operation of ICI (TR 1156). Work or conditions that resulted in financial benefit to ICI therefore resulted in financial benefit to Simpson.

152. Simpson, acting on behalf of ICI, loaned money from ICI to his children and, on at least one occasion, to himself (TR 819, 898, 1147-48; GX 27). Both Simpson and his family therefore derived personal benefit from ICI's receipt of income.

153. From July 1, 1988 until at least March, 1990, ICI had a contractual relationship with another insurance company, Worthington Insurance ("Worthington") of Bothell, Washington, whereby ICI received moneys when Cascade purchased its own insurance, such as

insurance on Cascade's buildings and automobiles, mortgage interest insurance, insurance for boilers and machinery, financial institution bond insurance and commercial package insurance, from Worthington (GX 25, 42).

154. Pursuant to the relationship between ICI and Worthington referred to in paragraph 93 above, Worthington paid ICI $4936.56 on June 28, 1989 (GX 42).

155. ICI's only function was to collect the commissions referred to in paragraphs 86 and 94, above. ICI maintained separate corporate and insurance licenses and purportedly negotiated as an independent entity the contractual arrangements with Family Life and Worthington referred to in paragraphs 88 and 93, above (TR 1154-55).

156. ICI performed no function or services with regard to the individual policies from which ICI received commissions (TR 1155).

157. From January 1, 1981 through at least March, 1990, ICI had no employees and no separate corporate offices. ICI's mailing address was Cascade's home office in Everett (TR 1136-37).

158. Federal and state law permitted Cascade to form a subsidiary which could have performed the same functions as ICI (TR 699-702; GX 43, 50).

159. Cascade was already absorbing most of the cost of operating such a company, as its employees were performing the work for which ICI received money. The only additional costs it would have incurred from operating a company which performed the same functions as ICI would

have consisted of application fees for federal authorities, registration and incorporation fees for state authorities, and separate signs and stationary (TR 700-701; GX 50).

160. Neither State nor Federal law requires that such a subsidiary be housed in a building separate from Cascade's office (TR 701; GX 50).

161. From 1981 through 1990, ICI was receiving an average annual income of $16,000 from Family Life (GX 32-41).

162. Based on this amount of income alone, and the low cost of forming a corporate subsidiary, such a subsidiary, had Cascade chosen to form one, would have been profitable (TR 708).

163. The minutes from Cascade's Board of Director's meetings from January, 1980 through March, 1990,

contain no reference to any discussion, resolution, consideration, report or vote concerning the formation of an insurance subsidiary by Cascade (TR 986).

164. Several members of Cascade's Board of Directors had no knowledge of ICI or details of its operations (TR 106-07, 149-50, 192-93, 741).

165. Since Simpson's departure from Cascade, Cascade has taken steps to create a company like ICI to receive these commissions, including paying for one of its employees to become a licensed insurance agent and obtaining a corporate license but has not yet done so (TR 197-98, 612-13).

CONCLUSIONS

A. PROFIT-SHARING

166. Simpson's authorization of the release of $529,500 in payments under the

Plan when he knew that Cascade was failing regulatory capital requirements; that Cascade was facing substantial writedowns in the value of various assets which would significantly affect the amount of profits available for payments under the Plan; that Cascade had already been directed by OTS to reduce by $1 million the value of Cascade's excess loan servicing fees; and that at least three members of Cascade's Board of Directors were concerned whether payments under the plan should not be made, amounts to an unsafe and unsound practice.

167. Simpson's conduct in authorizing release of the payments under the Plan, in terms of his personal receipt of $105,000 was also a breach of his fiduciary duty.

168. Simpson's receipt of the $105,000 payment he received under the Plan is unjust enrichment.

169. Simpson's intentional authorization for $105,000 to himself involved reckless disregard for safe and sound banking practices which are required by law and regulation. As well, his conduct was in reckless disregard of his fiduciary duty to Cascade. As to the remaining $424,500 that was paid to other Cascade employees, Simpson properly was concerned about future management performance. His conduct was not reckless as to payment to the others even though it was unsafe and unsound.

170. OTS has satisfied the elements of 12 U.S.C. §§ 1818(b) and (b)(6) and is therefore entitled to the issuance of an Order to Cease and Desist Directing

Restitution, ordering Simpson to cease and desist from unsafe and unsound practices, and directing restitution to Cascade of $105,000.

171. The $529,500 paid out under the Plan, which would not have been paid had Simpson waited for the final audited figures of Cascade's profits for 1989, represented a loss of contribution to the retained earnings or capital of Cascade.

172. The $105,000 Simpson personally received under the Plan was pecuniary gain to Simpson.

173. Simpson's conduct in authorizing release of the $529,500 paid under the Plan, which resulted in his own receipt of $105,000, was a form of self-dealing. Such conduct, in the face of the repeated cautions Simpson had concerning distribution of payments under

the Plan, was also contrary to a standard of personal integrity and honesty.

174. Simpson's conduct in intentionally authorizing the $105,000 paid to himself under the Plan, when he knew Cascade was capitally deficient and would have reduced profit for 1989, involves a willful disregard for the safety and soundness of Cascade.

175. OTS satisfies the elements of 12 U.S.C. § 1818(e)(1) and is therefore entitled to the issuance of an Order of Prohibition against Simpson.

176. Simpson's unsafe and unsound practice and breach of his fiduciary duty to Cascade was committed knowingly and recklessly.

177. As a result of Simpson's actions, Cascade experienced the loss of

a substantial contribution to its retained earnings or capital account.

178. OTS satisfies the elements of 12 U.S.C. § 1818(i) and is therefore entitled to the issuance of an Order Assessing Civil Money Penalty against Simpson of $105,000 and 12 U.S.C. § 1818(b) for an Order to Cease and Desist requiring restitution by Simpson of $105,000. (The penalty is separate from restitution but fits the circumstances.)

B. THE PREVIS LOAN

179. Simpson's receipt of the proceeds from the sale of his yacht to Randy Previs without even paying a commission on the sale in connection with the loan from Cascade to Randy Previs amounts to the receipt of a loan

procurement fee, and thus violates 12 C.F.R. § 563.40(b).

180. Simpson's personal involvement in the approval of a risky loan from which he stood to gain personally, his vote to approve this loan and his failure to notify Cascade's Board of Directors of all relevant facts he knew of this loan is a conflict of interest, which is inherently unsafe and unsound and a breach of Simpson's fiduciary duty to Cascade. In this regard, it defies belief that Simpson was unaware of the Previs bankruptcy. I conclude that if he did not know, he breached his fiduciary duty in not seeking to know. It is one thing not to participate in the approval of the loan and quite another to pretend ignorance or to actively seek it

(ignorance). His conduct was at least willfully reckless.

181. As a result of Simpson's unsafe and unsound reckless conduct and breach of fiduciary duty, Cascade suffered a loss of 328,424.

182. OTS satisfies the elements of 12 U.S.C. §§ 1818(b) and is entitled to an Order to Cease and Desist requiring restitution of $328,429 for his reckless conduct, his violating of 12 C.F.R. §§ 563.40(b), and his unsafe and unsound practices.

183. Simpson's receipt of benefit from his conduct, at the expense of Cascade, is a form of self-dealing, and as such involves personal dishonesty.

184. OTS satisfies the elements of 12 U.S.C. § 1816(e)(1), and is therefore

entitled to the issuance of an Order of Prohibition against Simpson.

C. **INSURANCE COMMERCE, INC.**

185. Simpson's use of Cascade employees during Cascade work hours for the benefit of ICI violated 12 C.F.R. § 563.33(b) and as well Simpson's fiduciary duty to Cascade. He used Cascade workers, Cascade office space, Cascade telephones, Cascade records and Cascade goodwill to make a good profit for himself.

186. Simpson's operation of ICI for his personal benefit and for that of his family when Cascade could have formed a subsidiary to receive the commissions paid to ICI, whether or not such a subsidiary would have of practical advantage to Cascade, represents a conflict of interest, which is inherently

unsafe and unsound, unjust enrichment and a willful breach of his fiduciary duty to Cascade.

187. The $161,522 received by ICI, to the benefit of Simpson, which could have been earned by a Cascade subsidiary in the 1980's, is unjust enrichment to Simpson. Of this amount, a conservatively estimated amount of $13,013 was received after the effective date of FIRREA in 1989.

188. OTS has satisfied the elements of 12 U.S.C. §§ 1818(b) and is therefore entitled to the issuance of an Order to Cease and Desist Directing Restitution, ordering Simpson to cease and desist from unsafe and unsound practices and directing restitution to Cascade of $161,522.

189. The money which ICI received, to the benefit of Simpson, could have been available to a subsidiary of Cascade, and as such the $161,522 income received by ICI from Family Life and Worthington from January, 1981 through March, 1990, is loss to Cascade and a gain to Simpson or his charity.

190. Simpson's receipt of $161,522 at Cascade's expense is a form of self-dealing and unjust enrichment.

191. Simpson's intentional operation of ICI and receipt of financial gain from its activities when Cascade could have received such benefit is a willful disregard for the safety and soundness of Cascade.

192. OTS has satisfied the elements of 12 U.S.C. § 1818(e)(1) and is entitled

to the issuance of an Order of Prohibition against Simpson.

193. Simpson's intentional operation of ICI is a breach of his fiduciary duty to Cascade.

194. Simpson's intentional operation of ICI, which resulted in substantial material benefit to himself and loss to Cascade, is a knowing and reckless cause of such gain and loss.

195. OTS satisfies the elements of 12 U.S.C. § 1818(i) also is therefore entitled to the issuance of an Order Assessing a Civil Money Penalty against Simpson for $13,013.

196. OTS, having met the elements of 12 U.S.C. § 1818(i) also is entitled to have the reasonable estimate of the cost of the investigation of this matter to United States Government, which OTS has

set at $20,000, included in the Assessment of a Civil Money Penalty.

197. OTS is entitled to the issuance of an Order Assessing a Civil Money Penalty against Simpson in the total

amount of $138,013**/, and Order of

**/A civil money penalty (CMP) is in fact punishment. Punishment should fit the circumstances. OTS introduced evidence at the hearing that Respondent received $105,000 pursuant to the profit-sharing plan after the effective date of FIRREA, August 9, 1989, when OTS received the authority to assess civil money penalties. OTS also introduced evidence that ICI, controlled by Respondent, received over $24,500 in 1989 and 1990. (GX 40, 41) Although the amount of money actually received by ICI after August 9, 1989 is uncertain, OTS included $13,013, a reasonable representation of that amount. Finally, OTS introduced evidence that the reasonable estimate of the cost of this investigation to the United States government was $20,000. (GX 49) The sum of these figures is $138,013, or $3,700 more than the Notice of Assessment of CMP dated February 12, 1991. (I know of no amendment.) Basically, the numbers, other than the estimate of the government's investigation cost, were specifically set out in the Notice. I conclude that the CMP is reasonable and warranted. Simpson merits the punishment but nonetheless, assessment of the investigative cost to the government appears somewhat new for an administrative proceeding. I find no reason to reject payment of the administrative cost component of the CMP. It is noted however that a "means" test of wealth is applied to a respondent that

(continued...)

Restitution of $594,946.

[**]/(...continued)
prevails in a Federal proceeding under what is called the Equal Access to Justice Act.

UNITED STATES OF AMERICA
Before The
OFFICE OF THRIFT SUPERVISION
DEPARTMENT OF THE TREASURY

In the Matter of	)	
	)	**Re: OTS AP 91-6**
JESS T. SIMPSON,	)	
	)	**Dated:**
Former President and Chairman of the Board of Directors	)	**February 12, 1991**
	)	
Cascade Savings Bank Everett, Washington	)	
	)	

ORDER

Under a new (November 1991) Federal statute dealing with funding of the Federal banking deposit insurance program, I am led to believe that Congress has mandated an easier standard for computing capital of a savings institution which earns a major portion of its income from the servicing of loans. Inasmuch as one of the key issues in this matter relates

to the amount of income properly earned by Cascade from loan servicing, it may be that the new statute has considerable relevance to this proceeding. In this regard, it is the position of former Cascade President Simpson that a 1989 formula for determining the proper amount of income from loan servicing involved an esoteric exercise where there was a reasonable basis for differing opinions.

Although closing briefs already have been filed in this matter, Simpson may be required to pay a civil money penalty of over $105,000 based in part upon his views on computing Cascade's loan servicing income and as well pay restitution of more than $529,000 for a profit sharing distribution made by Cascade based again in part on Simpson's views as described.

In these circumstances, the proceeding is reopened for the limited purpose of receiving written statements from the parties concerning the new legislation referred to above. Such written statements are due December 30, 1991. My decision due date will be adjusted accordingly.

/s/ Paul S. Cross
By Paul S. Cross, Administrative Law Judge, on December 10, 1991.

157321.2

APPENDIX C

UNITED STATES OF AMERICA
Before the
OFFICE OF THRIFT SUPERVISION

In the Matter of	
JESS T. SIMPSON,	**Re: OTS AP 91-6**
Former President and Chairman of the Board of Directors	**Dated: February 12, 1991**
Cascade Savings Bank Everett, Washington	**OTS ORDER No. AP 92-123** **Dated: November 18, 1992**

DECISION AND ORDER

TABLE OF CONTENTS

I. INTRODUCTION AND SUMMARY OF CONCLUSIONS C-4

II. BACKGROUND C-8

A. Summary of the Administrative Proceedings C-8

B. Summary of the Facts . . C-11

1. Profit-Sharing Distribution C-12
2. Previs Loan C-18
3. Insurance Operations C-23

C. The ALJ's Recommended Decision C-26

III. ISSUES FOR DECISION C-29

IV. DISCUSSION C-30

A. Standards Governing Restitution C-30

1. Profit-Sharing . . . C-39
2. Previs Loan C-54
3. Insurance Operations C-64

B. Removal and Prohibition Authority C-67

5 C. Civil Money Penalty Analysis C-70

1. Standards Governing the Imposition of CMPs C-70
2. Review of the Recommended CMP Amount C-72

V. CONCLUSION C-74

VI. ORDER C-75

DECISION

I. INTRODUCTION AND SUMMARY OF CONCLUSIONS

This case presents self-interested conduct that breached fundamental fiduciary duties of loyalty and care, thereby undermining an institution's safety and soundness and increasing the potential exposure of the Federal deposit insurance funds. Respondent Jess T. Simpson ("Simpson" or "Respondent") was, at all times relevant to this Decision and Order, the President and Chairman of the Board of Directors of Cascade Savings Bank of Everett, Washington ("Cascade" or "Association"). The record conclusively demonstrates Simpson's deliberate manipulation of Cascade for his personal benefit in defiance of his fiduciary responsibilities to the Association.

First, by directing payments in excess of $500,000 to himself and others at Cascade under the Association's profit-sharing plan, Simpson drained the Association of these funds even though he knew that it was undercapitalized and would be required to take substantial write-downs on certain assets. Second, Simpson caused Cascade to make a risky loan, demonstrably unsafe and unsound from its inception, as the quid pro quo for the borrower's agreement to purchase Simpson's own luxury boat. Finally, Simpson used Cascade and its employees to generate profits for another company he owned, thereby usurping business opportunities that he should have made available to Cascade as well as taking unlawful advantage of his position with the Association.

The conduct amply justifies the issuance of a cease and desist order against Respondent. The other issues presented concern the appropriate remedies for Simpson's unlawful conduct.

To issue a cease and desist order requiring restitution under 12 U.S.C. § 1818(b)(6)(A), the Office of Thrift Supervision ("OTS") must find that a respondent has been "unjustly enriched" in connection with a violation or practice, or has committed a violation or practice involving "reckless disregard" for the law, any applicable regulation, or a prior agency order. The Director of the OTS ("Director") concludes that the Respondent is liable for restitution under this standard. With respect to the profit-sharing distribution, the Director finds that the Administrative Law Judge ("ALJ")

improperly construed the two statutory bases for restitution. The Order accompanying this Decision increases the aggregate amount of the restitution from the ALJ's recommended amount of $594,946 to $1,009,446. The restitution reflects the full amount of the improper profit-sharing distribution ($529,500); Cascade's losses on the unsafe and unsound loan made in return for the sale of Simpson's boat ($318,424); and insurance commissions received by Simpson between 1981 and 1990 ($161,522).

This Decision also addresses the amount of the civil money penalty ("CMP") that may be imposed on the Respondent. The Director concludes that the record in this case is inadequate to support the imposition of CMPs and, accordingly,

declines to impose the CMPs recommended by the ALJ.

The remedies imposed by today's Order include: a cease and desist order directing Respondent to make restitution in the total amount of $1,009,446 to Cascade; and a prohibition order precluding the Respondent from participation in the conduct of the affairs of Cascade and any institution or entity listed in 12 U.S.C. § 1818(e)(7)(A).

II. BACKGROUND

A. Summary of the Administrative Proceedings

On February 12, 1991, the OTS Office of Enforcement ("Enforcement") issued a Notice of Charges and Hearing for an Order to Cease and Desist and to Direct Restitution and Other Affirmative Corrective Relief, Notice of Intention to

Prohibit, and Notice of Assessment of Civil Money Penalty (the "Notice"). The Notice alleges that Simpson engaged in numerous unsafe and unsound practices, violated regulations and statutes, and violated his fiduciary duties to Cascade. The Notice seeks an order to cease and desist and directing restitution, an order of prohibition, and civil money penalties.[1/] On February 12, 1991, the Director also issued a Temporary Order to Cease and Desist. In compliance with this Temporary Order, Simpson posted approximately $950,000 as security for any restitution that he might be required to pay.

[1/] See 12 U.S.C. §§ 1818(b) (cease and desist authority), 1818(e) (removal and prohibition authority), and 1818(i) (civil money penalty authority).

Simpson timely filed an answer to the Notice. A hearing was conducted on August 26-31, 1991 in Seattle, Washington.[2/] Opening briefs and proposed findings of fact and conclusions of law were filed by the parties under 12 C.F.R. § 509.27 (1991). The parties also filed reply briefs.

The ALJ's Recommended Decision, including Findings of Fact and Conclusions of Law (the "Recommended Decision"), and Recommended Order were served on the parties on December 23, 1991. Respondent filed exceptions to the Recommended Decision on January 21, 1992. Enforcement filed exceptions to the Recommended

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[2/] The hearing on the civil money penalty assessment was consolidated with the hearing on the underlying charges contained in the Notice.

Decision on January 23, 1992.[3] On March 16, 1992, the parties were notified that the Recommended Decision had been submitted for the Director's review and final determination. 12 C.F.R. § 509.32(b) (1991). The Director has entered Orders extending the time for issuance of the Final Decision until November 18, 1992.[4]

B. Summary of the Facts

At all times pertinent to this proceeding, Cascade was a state-chartered

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[3] On January 27, 1992, Enforcement requested expedited review of the Recommended Decision and issuance of a Final Decision and Order by February 28, 1992. The Director denied this request on February 24, 1992.

[4] See OTS Order No. AP 92-59 (June 12, 1992); OTS Order No. AP 92-73 (July 28, 1992); OTS Order No. AP 92-99 (September 18, 1992); Order No. AP 92-102 (October 2, 1992); Order No. AP 92-108 (October 9, 1992); Order No. AP 92-113 (October 23, 1992); and Order No. AP 92-120 (November 6, 1992).

federally-insured mutual savings and loan association.[5] Simpson served as President and Chairman of the Board of Directors throughout the relevant period.[6] The factual bases for the conclusions reached and the remedies imposed by the Director are next described.[7]

1. **Profit-Sharing Distribution**

In 1989, Cascade's profit-sharing plan provided for the distribution of one-half of annual pre-tax net profits in excess of $2 million to participating managers and officers. Distributions

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[5] On September 16, 1992, Cascade converted from a mutual to a stock institution.

[6] Simpson resigned as an officer and director of Cascade on March 13, 1990.

[7] The Notice recited an additional basis for the proceeding, Cascade's payment of educational expenses incurred by Simpson's family members. This charge was resolved prior to the hearing.

under the plan were determined by the Board of Directors' Compensation Committee, which consisted of Simpson and two other directors. In past years, distributions under the plan had been made at year end. The Compensation Committee reported scheduled profit-sharing distributions to the full Board of Directors at a regularly scheduled board meeting on December 12, 1989.

Cascade's internal profit projections dated December 12, 1989, indicated that Cascade would earn $4.14 million in pre-tax profits for 1989. If that projection had been accurate, then $1.07 million would have available under the distribution formula.

On November 22, 1989, however, the OTS had informed Simpson that Cascade had overvalued its excess loan servicing

account by approximately $1 million. This adjustment was not reflected in the December 12, 1989 profit projections.

Within a matter of days after the December 12, 1989 Board meeting, on December 15 and 20, 1989, Cascade's auditor, KPMG Peat Marwick ("Peat Marwick") also notified Cascade and Simpson that significant adjustments to the value of Cascade's excess loan servicing would be required. Preliminarily, Peat Marwick indicated that this asset was overvalued by $2.5 million ($780,000 for loans generated in 1989, and $1.7 million for loans generated in prior years). Peat Marwick also indicated that adjustments to other assets would be required. Although specific numbers were not provided, the auditor stated that these additional adjustments would also be

substantial. It was clear at that time that the auditor's recommended adjustments would bring the 1989 profits under the $2 million profit-sharing threshold.[8/]

On December 28, 1989, the OTS issued a directive requiring Cascade to record an adjustment of $1 million to the excess loan servicing account to reflect loans recorded since June 1989. The OTS directive also ordered Cascade to review accounting for other excess loan servicing. Cascade received this directive on December 29, 1989.

On that same day, despite the foregoing notices of substantial write-

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[8/] Additionally, Peat Marwick had previously recommended that Cascade establish general loan loss reserves. (Cascade had classified assets and was required by 12 C.F.R. § 563.160(d) to create a general loan loss reserve.) Cascade, however, had not created such a reserve by year's end.

downs to the value of assets that would reduce the projected net profits below the $2 million profit-sharing threshold, Simpson directed a profit-sharing distribution of $529,500; he personally received $105,000 of this distribution.

Cascade's audited financial statements for the year ended December 31, 1989, made available in April 1990, ultimately showed net profits before taxes for 1989 of $918,667. The audited financial statements included write downs of $1.25 million for excess loan servicing, $135,000 for loan origination fees, and $125,000 for purchased servicing. The audited statements also reflected the creation of $325,000 in specific loan loss reserves and $550,000 in general loan loss reserves. Thus, for 1989, Cascade in fact had not met the

$2 million threshold,[9] and the profit-sharing distribution was insupportable.

This distribution was also made at a time when Simpson knew that Cascade had insufficient capital. The OTS had notified Cascade and Simpson on several occasions in October and November 1989 that the Association was not meeting its capital requirements, specifically the risk-based capital requirement.[10] As a

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[9] To compare fairly the audited financial statement's figure of net profits before taxes ($918,667) with Cascade's internal $4.14 million pre-tax net profit projection, the profit-sharing distribution ($529,500) and a separate pool of bonus funds ($205,500) must be added to the $918,667. The total ($918,667 + $529,500 + $205,500 = $1.65 million) does not meet the $2 million threshold level that triggered profit-sharing.

[10] The Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 (1989) ("FIRREA") contained new minimum capital requirements. An interim final regulation

(continued...)

result, Cascade was required to submit a capital plan to OTS. By the time of the hearing in this case, Cascade had not remedied its capital deficiency and continued to operate under an approved capital plan. Simpson's conduct in authorizing the profit-sharing distribution in the face of all of this information reflected a sacrifice of his duties of loyalty and care to Cascade in favor of a single-minded orientation to his own self-interest.

2. **Previs Loan**

Simpson also caused Cascade to approve an unsafe and unsound loan to Randy Previs ("Previs"), one that had been rejected by over twenty other lending

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[10/](...continued)
implementing these requirements became effective on December 7, 1989. Regulatory Capital, 54 Fed. Reg. 46845 (November 6, 1989).

sources. Simpson provided the loan in exchange for Previs' purchase of Simpson's yacht. Simpson also received a loan procurement fee from Previs in making this loan. In involving himself in the initiation and approval of this loan, Simpson violated his fiduciary duties of loyalty and due care by placing his self-interest before the interests of the Association, which caused Cascade to suffer a substantial loss.

In 1975, Previs purchased the Valley View Ranch, a 66-acre parcel of land located in Thorp, Washington. Previs filed for bankruptcy in February, 1980, and wanted to obtain financing to buy back the Ranch.

In 1981, Previs sought a real estate loan from Cascade. He was in bankruptcy and had a credit record that noted the

bankruptcy, an adverse judgment for $60,000, and other items reflecting a poor credit history. At the time Previs applied to Cascade, over twenty other lenders had turned down his application. The security property was located outside of Cascade's usual lending area and was non-revenue producing rural land on which Cascade typically did not extend credit.

Previs occasionally bought large pleasure boats to refurbish and resell at a profit. At the suggestion of a yacht broker, Previs contacted Simpson. Simpson agreed that Cascade would make the real estate loan, if Previs agreed to purchase Simpson's yacht. Thereafter, Previs applied to Cascade for the loan on the Ranch. The loan was processed on an expedited basis, approved by a three-member loan committee including Simpson,

and ratified by Cascade's Board of Directors. On April 29, 1981, a 90-day loan for $258,000 was issued to the Katie Previs Land Co., with Randy Previs and his wife Katie Previs signing as principals.

Although Cascade's Board of Directors ratified the initial loan (and subsequent refinancings, discussed below), Simpson never informed the Board of certain material information about the loans including the facts that Previs was in bankruptcy, that Simpson was negotiating the sale of his yacht to Previs, and that Simpson subsequently sold the yacht to Previs in July 1981 in return for initiating and recommending the approval of the real estate loan.

On June 19, 1981, Cascade refinanced the loan. As a part of this refinancing, Previs received an additional $50,000.

From this amount, Previs used $20,000 to pay Simpson's commission to the yacht broker, and $30,000 to pay for materials to renovate the yacht. On July 1, 1981, the Previs Equipment Company, with Randy and Katie Previs signing as principals, contracted to purchase the yacht from Simpson in return for a $180,000 note. Within 6 months Previs had renovated the yacht, sold it at a profit, and repaid the note to Simpson.

Previs' real estate loan was refinanced by Cascade again on April 20, 1982. Despite his payments to Simpson, Previs never made any payments on the loans to Cascade. Cascade filed a lawsuit to foreclose on the property on January 25, 1983. The total loss suffered

by Cascade when the Ranch was finally sold was $318,424.[11/]

3. Insurance Operations

Between 1981 and 1990, Cascade provided lists of new mortgage borrowers to Family Life Insurance Company ("FLI"), a company in which Simpson had no interest. FLI then attempted to sell mortgage life insurance to these borrowers. FLI split its commissions on the sale of this insurance on a 50-50 basis with Insurance Commerce Inc. ("ICI"), a company controlled by Simpson. In exchange, ICI was to collect the

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[11/] The amount outstanding on the note when foreclosure proceedings began was $538,424. Government Exhibit ("GX") 17. After foreclosure, Cascade ultimately sold the property on September 27, 1988 for $210,000. GX 22. The difference is $328,424. For the reasons described in Section IV.A.2., however, the Director has reduced this amount by $10,000 to $318,424.

premiums on the policies for FLI. In fact, ICI had no employees and it was Cascade employees who collected insurance premium payments along with the borrowers' monthly mortgage payments, and remitted the premium payment to FLI. During 1981-90, ICI received a total of $156,586 in commissions from FLI for these services by Cascade employees.

From 1988 through 1990, Cascade paid premiums to Worthington Insurance Company on various business policies insuring Cascade. Pursuant to an agreement with Worthington, ICI received commissions of at least $4,936 on these policies because ICI, acting through Simpson, sent this business to Worthington.[12/]

[12/] Additionally, ICI was entitled to receive commissions when it generated orders for insurance coverage from Worthington. Cascade employees referred (continued...)

ICI held appropriate licenses but performed no function other than to receive commissions from FLI and Worthington. It did not pay Cascade for the services of Cascade's employees.

At all relevant times, Cascade was not legally prevented from forming a subsidiary to perform the functions performed by ICI. Based on the income derived by ICI, such a subsidiary would have been profitable. The role Simpson engineered for his companies at the expense of Cascade's business opportunities constituted another breach of Simpson's fiduciary duty of loyalty.

12/ (...continued)
potential customers by directly filing referral lists with Worthington. The record, however, does not show whether commissions were generated from these referrals.

C. The ALJ's Recommended Decision

The ALJ determined that the release of the $529,500 in profit-sharing to Cascade management was an unsafe or unsound practice; and that Simpson's authorization of the payment of $105,000 to himself breached his fiduciary duty to Cascade, was in reckless disregard of safe and sound banking practices, and unjustly enriched Simpson by $105,000. Accordingly, the ALJ recommended a cease and desist order directing restitution of $105,000 under 12 U.S.C. § 1818(b). The ALJ found that the $424,500 payment to other managers did not meet the reckless disregard standard under the statutory restitution provision, 12 U.S.C. § 1818(b)(6)(A), and he did not recommend restitution of this amount. Additionally, the ALJ found that Simpson's conduct

satisfied the requirements for issuance of an order of prohibition under 12 U.S.C. § 1818(e), and recommended that the Director impose a prohibition order against Simpson. The ALJ also recommended a Tier Three CMP of $105,000 under 12 U.S.C. § 1818(i) in connection with the profit-sharing distribution.

The ALJ further determined that Simpson received a loan procurement fee in connection with the Previs loan, contrary to 12 C.F.R. § 563.40. The ALJ also found that Simpson breached his fiduciary duty and engaged in unsafe and unsound practices by approving a risky loan when he stood to gain financially, and by failing to inform the Board of Directors of all material facts associated with the loan. For these violations, the ALJ recommended a cease and desist order

directing restitution of $328,424. The ALJ again recommended an order of prohibition against Simpson under 12 U.S.C. § 1818(e).

The ALJ found that Simpson violated his fiduciary duty to Cascade by permitting ICI's uncompensated use of Cascade's employees during Cascade's work hours. He also found that Simpson violated 12 C.F.R. § 563.33(b), which prohibits savings associations from permitting salaried employees or officers to work during office hours for other affiliated entities without compensation from that entity. The ALJ further determined that Simpson's operation of ICI for personal benefit while Cascade could have formed a similar organization was, in addition to a violation of his fiduciary duty, a conflict of interest, an unsafe or

unsound practice, and a usurpation of Cascade's corporate opportunities. For these violations, the ALJ recommended an order to cease and desist directing restitution of $161,522; an order of prohibition against Simpson; and CMPs of $13,013.[13/]

III. ISSUES FOR DECISION

This proceeding presents two main issues: (1) What standards are appropriate to determine whether Respondent was "unjustly enriched" or acted with "reckless disregard" for the

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[13/] Enforcement introduced evidence that ICI, controlled by Simpson, received over $24,500 in 1989 and 1990. GX-40, 41. The ALJ estimated that $13,013 of the $24,500 was received after August 9, 1989.

In addition to the CMPs ordered as a result of the profit-sharing agreement ($105,000) and the ICI transactions ($13,013), the ALJ included in the CMP $20,000 which represented the cost of investigation by the United States Government.

law, applicable regulations, or prior OTS orders for the purposes of ordering restitution under 12 U.S.C. § 1818(b); and (2) May the Director order civil money penalties under 12 U.S.C. § 1818(i) against the Respondent when neither Enforcement nor the ALJ specifically addressed the statutory mitigating factors that the Director is required to consider?

IV. DISCUSSION[14/]

A. Standards Governing Restitution

Under 12 U.S.C. § 1818(b)(1), the OTS may issue a cease and desist order if an

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[14/] Exceptions that are not specifically addressed in this Decision are denied.

In his exceptions, Respondent attempted to incorporate by reference arguments made in prior pleadings. Respondent's failure to clearly identify issues for review constitutes a waiver of objection under 12 C.F.R. § 509.29(b) (1991). Objections contained in these general exceptions, therefore, are deemed waived.

institution-affiliated party[15] has engaged in proscribed activities including: engaging in an unsafe or unsound practice in conducting the business of the association;[16] or violating a law, rule or regulation, or conditions imposed in writing or written agreements with the agency. The OTS may require the institution-affiliated party to cease and desist from the violation or practice and

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[15] Simpson, as President and Chairman of Cascade's Board of Directors, is an institution-affiliated party under 12 U.S.C. § 1813(u).

[16] Unsafe and unsound practices, for the purposes of the issuance of a cease and desist order, involve conduct that is contrary to generally accepted standards of prudent operation of a financial institution, the possible consequence of which, if continued, may be abnormal risk, or loss or damage to an institution, its shareholders, or the Federal deposit insurance funds. See In the Matter of Neil M. Bush, Final Decision and Order, OTS Order No. AP 91-16, at 30-31 (April 18, 1991).

to take affirmative action to correct the conditions resulting from the violation or practice. 12 U.S.C § 1818(b)(1) and (6). The OTS may order an institution-affiliated party to make restitution or provide reimbursement, indemnification, or guarantee against loss, if certain standards, discussed below, are met. 12 U.S.C. § 1818(b)(6)(A). The OTS may also take such other action as it determines to be appropriate. 12 U.S.C. § 1818(b)(6)(F).

To support an order requiring restitution under 12 U.S.C. § 1818(b)(6)(A), Enforcement must demonstrate: (1) that the Respondent was unjustly enriched in connection with the violation or practice with respect to which the cease and desist order is issued; or (2) that the violation or

practice involved a reckless disregard for the law or any applicable regulations or prior order of the appropriate Federal banking agency. While the ALJ made findings with respect to each of these elements, he did not define the terms "unjust enrichment" and "reckless disregard."

"Unjust enrichment" and "reckless disregard" are not defined in the statute. Recent case law, however, establishes that the term "unjust enrichment" should be construed broadly to occur when a respondent gains "a significant personal benefit" through unlawful means. Akin v. Office of Thrift Supervision, 950 F.2d 1180 (5th Cir. 1992) (Respondent received significant personal benefit by retaining and disposing of funds that he would otherwise be required to contribute to the

association under a net worth maintenance agreement; this personal benefit was sufficient to support a conclusion that he was unjustly enriched).

The alternative standard for directing restitution, "reckless disregard," has not been addressed in agency decisions or case law interpreting 12 U.S.C. § 1818(b)(6). However, case law under other federal statutory schemes is instructive on the meaning of "reckless." In reviewing an action under Rule 10b-5, the United States Court of Appeals for the Seventh Circuit defined recklessness as "'an extreme departure from the standards of ordinary care, and which presents a danger . . . that is either known to the defendant or that is so obvious that the actor must have been aware of it.'" Sundstrand Corp. v. Sun Chemical Corp.,

553 F.2d 1033, 1045 (7th Cir. 1977), cert. denied 434 U.S. 875, 54 L.Ed.2d 155, 98 S.Ct. 225 (1977), quoting Franke v. Midwestern Oklahoma Development Authority, 428 F.Supp. 719 (W.D. Okla. 1976), vacated on other grounds, 619 F.2d 856 (10th Cir. 1980).[17] The Seventh Circuit explained:

> Indeed, the Franke definition of recklessness should be viewed as

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[17] The standard of recklessness articulated by the Seventh Circuit has been followed by the majority of the circuits. See Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1569 n.8 (9th Cir. 1990), cert. denied, ____ U.S. ____, 111 S.Ct. 1621, 113 L.Ed.2d 719 (1991); Hackbart v. Holmes, 675 F.2d 1114, 1118 (10th Cir. 1982); SEC v. Carriba Air, Inc., 681 F.2d 1318, 1324 (11th Cir. 1982); Broad v Rockwell Int'l Corp., 642 F.2d 929, 961-62 (5th Cir. 1981); cert. denied, 454 U.S. 965, 102 S.Ct. 506, 70 L.Ed.2d 380 (1981); McLean v. Alexander, 599 F.2d 1190, 1197-98 (3rd Cir. 1979); Mansbach v. Prescott, Ball & Turben, 598 F.2d 1017, 1025 (6th Cir. 1979); Cook v Avien, Inc., 573 F.2d 685, 692 (1st Cir. 1978); Rolf V. Blyth, Eastmann Dillon & Co., 570 F.2d 38, 46-47 (2d Cir. 1978), cert. denied, 439 U.S. 1039, 99 S.Ct. 642, 58 L.Ed.2d 698 (1978).

> the functional equivalent of intent . . . . Under this definition, the danger of misleading . . . must be actually known or so obvious that any reasonable man would be legally bound as knowing, and the omission must derive from something more egregious than even "white heart/empty head" good faith. While this definition might not be the conceptual equivalent of intent as a matter of general philosophy, it does serve as a proper legal functional equivalent for intent, because it measures conduct against an external standard which, under the circumstances of a given case results in the conclusion that the reckless man should bear the risk of his omission. . . . When measured against this external standard, it may be said that such a reckless man has "use[d] or employ[ed] [a] deceptive device" within Section 10(b) [of the Securities Exchange Act of 1934]. Sundstrand, 553 F.2d at 1045 (citations and footnotes omitted).

A similar approach has been followed in reading a recklessness standard into § 6672 of the Internal Revenue Code, which

holds corporate officials liable for "willfully" failing to collect or pay taxes. In Sawyer v. United States, 831 F.2d 755 (7th Cir. 1987), the court said:

> A person acts willfully under § 6672 if his "conduct denotes intentional, knowing and voluntary acts. It may also indicate a reckless disregard for obvious or known risk." . . . Recklessness in this context is established if the corporate officer "(1) clearly ought to have known that (2) there was a grave risk that withholding taxes were not being paid and if (3) he was in a position to find out for certain very easily." 831 F.2d at 758 (citations omitted; emphasis in original).

The predecessor of the OTS ruled that "willful disregard" exists when an individual:

> a) purposely (as opposed to accidentally) commits an act and that act evidences neglect or lack of thoughtful attention to the institution's safety or soundness, or b) acts with plain

> indifference to the institution's safety and soundness . . . . [T]he only requirement is that the individual acted intentionally in committing the acts which constitute the violation and was aware of or knew what he was doing.

In the Matter of M, FHLBB Res. 89-537 at 51 (March 6, 1989). See also In the Matter of O'Keeffe, OTS Final Decision and Order, OTS Order No. 90-60, at 28-29 (April 26, 1990).

Accordingly, for the purposes of 12 U.S.C. § 1818(b)(6)(A), the Director concludes that reckless disregard for the law, applicable regulations, or an agency order exists when: (1) the party acts with clear neglect for, or plain indifference to, the requirements of the law, applicable regulations or agency orders of which the party was, or with reasonable diligence should have been,

aware; and (2) the risk of loss or harm or other damage from the conduct is such that the party knows it, or is so obvious that the party should have been aware of it.

In light of these standards, as well as well-established principles relating to unsafe and unsound practices and breach of fiduciary duty, the Director next analyzes each of the counts against Simpson.

1. **Profit-Sharing**

Before the Director may reach the issue of restitution, he must conclude that an unsafe or unsound practice has occurred or a violation was committed. In the case of the profit-sharing plan, it is clear that Simpson breached his fiduciary duties and engaged in unsafe and unsound practices.

As a director and officer of Cascade, Simpson owed a fiduciary duty of loyalty

to the institution. This duty requires directors and officers to administer the affairs of the institution with candor, personal honesty and integrity. They are prohibited from advancing their own personal or business interests, or those of others at the expense of the institution. In the Matter of Neil M. Bush, at 13-14. Under this fiduciary duty, directors and officers have a fundamental obligation "to avoid placing themselves in a position that creates, or that leads to or could lead to, a conflict of interest or appearance of a conflict of interest." Id. at 10-11; see 12 C.F.R. § 571.7(b). A director who may experience a direct or indirect benefit is required to abstain from participating in the matter in which he has a conflicting

interest and from voting on the matter. In the Matter of Neil M. Bush, at 20, 21.

Simpson violated his duty of loyalty by promoting his own interest as the major beneficiary under the profit-sharing plan ahead of the interest of the Association. Initially, Simpson directly and substantially participated in profit-sharing deliberations. He was one of three members of the Board of Directors' Compensation Committee that set the amount of the distributions to participants in the plan, including a $105,000 distribution to Simpson. As noted above, his duty of loyalty to the Association demanded that he abstain from participation in all profit-sharing discussions in which he had an interest. Moreover, Simpson advanced his own self-interest by authorizing the release of

profit-sharing payments, including his $105,000 payment. This action was detrimental to the Association's interest because it resulted in a substantial distribution of assets that was not required under the profit-sharing plan,[18] and because the payments impaired Cascade's ability to comply with regulatory capital requirements.[19] The

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[18] Respondent repeatedly asserts that the profit-sharing payment was a legitimate expense that could not be avoided by Cascade. A copy of the profit-sharing plan, if the plan was reduced to writing, was not placed into evidence. The parties, however, do not dispute the basic requirements of the plan including the $2 million profit-sharing threshold. Based on the description of the plan in the record, the audited financial statement, and the facts summarized above relating to Cascade's financial condition, the Director concludes that there was no obligation under the plan to make any profit-sharing payments.

[19] Simpson argues that approval of the profit-sharing distribution is unrelated to Cascade's capital position (continued...)

Director concludes that these actions constitute violations of Simpson's fiduciary duty of loyalty as defined in 12 C.F.R. § 571.7. His conduct also caused undue risk of loss to the institution and the insurance fund by improperly reducing the earnings of a capitally deficient institution and, thus, constitutes an unsafe and unsound practice that is sufficient to support a cease and desist order. See 12 C.F.R. § 571.7(b); In the Matter of Neil M. Bush, at 31-32.

In addition to the fiduciary duty of loyalty, directors of savings associations owe a fiduciary duty of care to the

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[19/](...continued)
and its safety and soundness because the plan was based on profit and not capital. This argument is mistaken. Absent the distribution, Cascade's net profits would have increased the amount of Cascade's retained earnings and reduced Cascade's capital deficiency, thereby advancing its safety and soundness.

institution. The Supreme Court has defined that duty as:

> [T]hat [degree of care] which ordinarily prudent and diligent men would exercise under similar circumstances, and in determining that, the restrictions of the statute and the usage of business should be taken into account.

Briggs v Spaulding, 141 U.S. 132 (1891). This duty requires directors to act diligently, prudently, honestly, and carefully to ensure their institution's compliance with state and Federal banking laws and regulations.[20] In the Matter of M, at 41-42. The director's duty of care

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[20] The performance of a director's responsibilities is fundamental to the safety and soundness of a Federally insured depository institution and the protection of the Federal insurance funds. Accordingly, OTS, as a Federal regulator obligated to protect the insurance funds, will not recognize state law that purports to limit the duties or liabilities of thrift directors. See In the Matter of Bush at 12-13.

includes: selecting, monitoring and evaluating competent management; establishing business strategies and policies; monitoring and assessing the program of business operations; establishing and monitoring adherence to policies and procedures required by statute, regulations and principles of safety and soundness; and making business decisions on the basis of fully informed and meaningful deliberations. Directors are also responsible for ensuring management's prompt response to and compliance with the supervisory directives of regulators."[21/]

[21/] See e.g., Corsicana National Bank v. Johnson, 251 U.S. 68 (1919) (approval and institution of loan policies and procedures); Bowerman v. Hamner, 250 U.S. 504, 513 (1919) (attendance at board of director meetings); Briggs, 141 U.S. at 162 (supervision of management); Brickner v. FDIC, 747 F.2d 1198, 1202 (8th Cir.

(continued...)

Officers are responsible for the day

[21/](...continued)
1984) (heeding the admonitions and warnings of supervisory authorities); FDIC v. Mason, 115 F.2d 548 (3rd Cir. 1940) (adherence to normal and prudent standards in the banking community); Atherton v. Anderson, 99 F.2d 883 (6th Cir. 1938) (supervision of management, selection of members of executive and loan committees, maintenance of an impartial and objective audit system, performance of periodic examinations of the institution, and review of loans, delinquencies, large lines of credit and problems loans); Goess v. Ehret, 85 P.2d 109 (2d Cir. 1936) (review of financial reports); and White v. Thomas, 37 F.2d 452, 454 (9th Cir. 1930) (general knowledge of the manner in which the thrift business is conducted).

The regulatory agencies and others have produced guides that provide useful advice on ways directors can fulfill their duties to the institutions they serve. These include: OTS Statement Concerning the Responsibilities of Directors and Officers of Insured Depository Institutions (November 16, 1992); OTS Regulatory Handbook on Thrift Activities, Section 140 (1990); OTS Director Information Guidelines (1989); Pocket Guide for Directors (FDIC, 1988); The Director's Handbook (OCC, 1987). See also, The Director's Guide: Role and Responsibilities of a Savings Institution Director (FHLB-SF, 1988).

to day management of the institution. As a result, an "inside" director, such as Simpson, generally has greater knowledge of, and direct responsibility for, the management of the institution. Officers are responsible for implementing the policies and business objectives set by the board and for running the day to day operations of the institution consistent with those policies and objectives and in compliance with the applicable laws, rules and regulations and the principles of safety and soundness. The officers must provide directors with timely and ample information so that directors may discharge their responsibilities.

Simpson's actions with respect to the profit-sharing distribution were also contrary to accepted standards of prudent operation of a financial institution, and

violated his duty of care to Cascade. Simpson made the profit-sharing distribution in the face of persistent warnings from Cascade's auditor and its regulator that substantial asset write-downs would be required, and despite admonitions that Cascade needed to enlarge its capital to comply with the statutory and regulatory minimum capital requirements under FIRREA. As a result, Cascade was exposed to excessive risk of loss or damage. Moreover, the profit-sharing distribution damaged the Association by substantially compromising its ability to comply with regulatory requirements. The Director concludes that Simpson's conduct violated his duty of care and constituted an unsafe and unsound practice.

Accordingly, the Director concludes that the requirements for the issuance of a cease and desist order under 12 U.S.C. § 1818(b) are met here. Restitution is appropriate if the requirements of 12 U.S.C § 1818(b)(6) are also met.

The ALJ determined, and the Director agrees, that the $105,000 distribution to Simpson was made with reckless disregard for the law.[22/] Simpson was plainly indifferent to the warnings of OTS and Cascade's auditor, and the size of the distribution and the thinness of Cascade's capital position persuade the Director that Simpson must have known that any distribution would damage the institution's capital position.

[22/] In addition, Simpson was clearly unjustly enriched in the amount of $105,000.

The ALJ also determined that the profit-sharing payment of $424,500 to Cascade managers other than Simpson was an unsafe and unsound practice but was not made in reckless disregard for the law. The ALJ found that the payment represented a proper balancing between Cascade's management needs and Cascade's capital needs. Recommended Decision at 26. Enforcement excepts to this finding.

The Director disagrees with the ALJ's conclusion that the $424,500 profit-sharing distribution to the other managers was not in reckless disregard for the law. Simpson's actions on this score reflect the same plain indifference to the warnings of OTS and Cascade's auditor that his acceptance of the $105,000 distribution does. Simpson was aware that Cascade was capital deficient. He also

knew that Cascade was subject to substantial write downs of several assets that would reduce pre-tax net profits below the $2 million profit-sharing threshold.[23/] That the release of the

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[23/] These adjustments included $1 million in write downs ordered by the OTS (reflecting excess loan servicing recorded since June 6, 1989) and additional adjustments necessary to reflect excess loan servicing recorded prior to that date. Peat Marwick had estimated that the total write down of this asset was nearly $2.5 million. The ALJ found that "Simpson believed that if the loan servicing were to be re-evaluated, then all aspects of the loan servicing should be re-evaluated, which would result in an offset to the write down envisioned by Peat Marwick." Recommended Decision at 24. This finding does not affect the determination that the distribution was made with reckless disregard. Simpson was aware that the OTS and Peat Marwick believed that this write down and other substantial adjustments (e.g., the creation of general and specific loan loss reserves) were necessary. Under these circumstances, Simpson should not have acted on the self-serving assumption that his belief would ultimately prevail over the position of the regulator and of Cascade's auditor.
(continued...)

profit-sharing payments would have a significant harmful effect on Cascade's ability to meet the capital requirements in OTS regulations was so obvious that Simpson must have or should have known of it, and he ignored this information in favor of an immediate profit-sharing distribution to others as well as to himself. Under these circumstances, the Director concludes that the profit-sharing payments were authorized by Simpson in reckless disregard for the law and that restitution is appropriate under 12 U.S.C. § 1818(b)(6)(A)(ii).[24] The Order entered

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[23] (...continued)
Rather, Simpson should have delayed the distribution and resolved the issues with the OTS and Peat Marwick, rather than take an unreasonable risk that profits over $2 million would be generated.

[24] Even if the Director agreed with the ALJ's conclusion that the distribution to other managers was not made in reckless (continued...)

today directs Simpson to make restitution of $529,500, the full amount of the profit-sharing distribution.[25]

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[24] (...continued)
disregard for the law or the regulations, restitution of the full amount of the distribution could still be ordered based on the alternative basis of unjust enrichment.

[25] FIRREA's restitution provisions do not limit restitution to the amount of an individual's personal gain, but rather are intended to recover the full amount of loss resulting from misconduct that produces a benefit for the wrongdoer. See H.R. Rep. No. 101-54(I) 101st Cong. 1st Sess. 392 (1989). Accordingly, the measure of recovery that may be ordered under the statute based upon either reckless disregard for law and applicable regulations or unjust enrichment is the amount of the loss to the association caused by the violation, or unsafe or unsound practice or breach, and is not limited to the amount of benefit to the respondent. The FDIC has reached a similar conclusion in In the Matter of Palmer, et al., FDIC-90-156 c&b, (Sept. 17, 1991).

2. Previs Loan

In connection with the Previs loan, Simpson received a loan procurement fee in violation of 12 C.F.R § 563.40.[26/]

[26/] Respondent argues that the Previs boat sale was an arms' length transaction for full value and, therefore, does not violate 12 C.F.R. § 563.40. Section (a) of this regulation bars affiliated persons from receiving any fee or other compensation--earned or unearned--in connection with the procurement of a loan. Section 563.40(b) extends additional prohibitions contained in the Real Estate Settlement Procedures Act of 1974 ("RESPA") to associations and affiliated persons with respect to loans on real property.

Respondent argues that he may rely on the exceptions that apply to RESPA coverage, including an exception for transactions involving bona fide compensation for goods or facilities actually furnished. Section 563.40(b) of the regulations incorporates only the prohibitions contained in RESPA. Section 563.40(b) was not intended to limit the unqualified language of Section 563.40(a). Section 563.40 applies to the Respondent's situation. United States v. Grissom, 814 F.2d 577, 579-80 (10th Cir. 1987). - Independently of this analysis, Respondent breached his fiduciary duties of loyalty,

(continued...)

Additionally, Simpson's involvement in the approval of the Previs loan constituted a breach of his fiduciary duty of loyalty as defined in 12 C.F.R § 571.7. As explained above, directors and officers of an association have a duty of loyalty to the association that they serve. The duty of loyalty demands that a director abstain from participating or voting on matters in which he or she has a conflict of interest. The duty of loyalty also requires the corporate fiduciary to disclose all material nonprivileged information relevant to a corporate decision from which he or she may derive a

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[26] (...continued)
candor and care by using the Previs loan application as a opportunity to secure the sale of his personal property while withholding key information from the directors, resulting in an unsound loan and a substantial loss to the institution.

personal benefit. In the Matter of Neil M. Bush at 17 and 21.

Simpson caused Cascade to approve a loan in which he stood to gain personally through the sale of his yacht. Rather than abstain from any involvement with the loan, Simpson actively sought its approval through such actions as sitting on the three-member loan committee that approved the loan. This self-dealing constitutes a clear conflict of interest and a violation of his duty of loyalty. Simpson also failed to disclose material information to the Board including his interest in the loan and information regarding Previs' bankruptcy. This lack of disclosure violated his obligation of candor, a further violation of his duty as a fiduciary. Based on the above, the Director concludes that Simpson's

participation in this matter was a breach of his fiduciary duty to Cascade, as defined in 12 C.F.R. § 571.7, and was an unsafe and unsound practice.

Further, Simpson violated his duty of care. Simpson supported and approved the Previs loan despite his knowledge that Previs was in bankruptcy. Information such as an adverse judgment of $60,000 and other evidence of poor credit history were contained in credit reports obtained by Cascade and available to Simpson. The facts that the property securing the loan was located beyond Cascade's usual lending area and was non-revenue producing rural property on which Cascade did not typically extend credit were, similarly, readily ascertainable. Because of these facts, Simpson exposed Cascade to an abnormal risk of loss or harm from the

loan and an unsafe and unsound practice, thereby breaching his duty of care. The Director concludes that this unsafe and unsound practice and fiduciary breach are sufficient to support the issuance of a cease and desist order.

Restitution is required in the case of this unsafe and unsound practice and unlawful act, on two alternative grounds. First, Simpson acted purposefully to ensure the approval of a high-risk loan in order to facilitate another transaction in which he had a personal interest. This is the clearest form of disregard of, and indifference to, the standards that govern a director's conduct. In light of his own conflict of interest and his knowledge of Previs' dubious financial position, Simpson knew or should have known that his actions exposed the Association to an

abnormal risk of harm or loss from the loan. The Director concludes that Simpson's participation in the Previs loan demonstrated reckless disregard for the law and the applicable regulations at 12 C.F.R. § 563.40. Accordingly, the Respondent is required to make restitution under 12 U.S.C. § 1818(b)(6)(A)(ii).

The Director also concludes that Simpson was unjustly enriched through his actions in the Previs transaction.[27/] Simpson received a benefit in connection with the initial financing because he was able to sell his yacht as a direct result of Cascade's origination of the loan. Simpson also received financial enrichment in connection with Previs' refinancing of the loan. His obligation to pay a yacht

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[27/] The ALJ made no finding with regard to unjust enrichment.

brokerage fee of $20,000 was satisfied as a result of this refinancing. Accordingly, the Director finds that Simpson was unjustly enriched and that the requirements for ordering restitution under 12 U.S.C. § 1818(b)(6)(A)(i) also are met by the initial Previs loan and by the refinancing.

The ALJ required Simpson to make restitution of Cascade's loss in the amount of $328,424. This amount was based on the amount outstanding on the note when foreclosure proceedings on the Previs property began ($538,424),[21] less the

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[21] This information was contained in GX 17, a recapitulation of the loan. The recapitulation summarizes voluminous loan documents to which Simpson was provided access. Simpson argues that the recapitulation is unreliable hearsay and is inadmissible.

The recapitulation is relevant and material to the issue of restitution, is (continued...)

amount received when the property was subsequently sold ($210,000).

Respondent argues that this calculation does not reflect accurately the loss to Cascade. Respondent points out that the ALJ's restitution computation does not take into account an agreement to sell the property to Dr. and Mrs. Larry Bundy for a purchase price of $350,000. The Bundy sale was not

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[28/](...continued)
not repetitious of other evidence, and is therefore admissible in OTS proceedings. 5 U.S.C. 556(d) and 12 C.F.R. § 509.24. While the OTS is not confined to the formal rules of evidence, it is instructive to note that the recapitulation is admissible in Federal court under Fed. R. Evid. 1006. That rule provides that contents of voluminous writings which cannot conveniently be examined in court may be presented in the form of a chart, summary or calculation, provided that the underlying information is available for examination and copying.

consummated, however, and the ALJ correctly excluded it from the calculation.[29]

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[29] Respondent also argued that the calculation does not reflect accurately the loss to Cascade because it:

-Includes loan fees and related charges of $43,092 that were not "out-of-pocket" losses to Cascade. These fees and charges represent the value of services rendered by Cascade in connection with the loans. To fully indemnify Cascade for the loss on the Previs loan, such services should be included in the restitution amount.

-Includes the payment of interest on the loan after the date of default. Although generally accepted accounting principles (GAAP) do not permit Cascade to recognize income from loans that are in default, GAAP has no bearing on the debtor's obligation to pay, or the association's right to receive such payments. Cascade may not book as income interest that is not paid on a loan in default, but that does not affect its legal entitlement to the interest payment.

-Compound interest. Each time the Previs loan was renewed, interest and loan fees were capitalized resulting in the compounding of interest. Simpson argues that compound interest is not permitted under Washington law, absent an express contract. Stauffel v. Northwestern Mutual

(continued...)

Simpson also argues that a down payment ($10,000) and loan extension fee ($10,000) paid by the Bundys should be deducted from the amount of the restitution. The ALJ declined to do so. The loan extension fee was not deducted because it represents the value of services rendered by Cascade in connection with the unconsummated transaction. The down payment, if retained by Cascade, may be considered an offset. Enforcement did not present any information refuting the evidence that Cascade received the down payment in connection with this sale, or

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[29/] (...continued)
Life, 184 Wn. 431, 436, 51 P.2d 390, 392 (1935). The cited case does not preclude the payment of compounded interest as restitution, but merely reflects the Washington courts' reluctance to create an obligation to require the payment of compound interest where a note or contract merely provides for the annual payment of interest.

indicating that Cascade did not retain the down payment. Accordingly, the restitution ordered is reduced by the $10,000 down payment to $318,424.

3. Insurance Operations

In connection with the insurance operations, the Director finds that Simpson: (1) usurped Cascade's corporate opportunities, see 12 C.F.R. § 571.9; (2) utilized Cascade employees during business hours in violation of 12 C.F.R. § 563.33; and (3) engaged in a conflict of interest which constituted a breach of his fiduciary duty of loyalty[30/] and an inherently unsafe and unsound practice (see 12 C.F.R. § 571.7). The requirements

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[30/] The fiduciary duty of loyalty is discussed above. Simpson's advancement of ICI's interest at the expense of Cascade's is an unambiguous breach of this duty.

for a cease and desist order therefore are met.

Between 1981 and 1990, Simpson received a substantial monetary benefit, in the amount of $161,522, from his conduct in connection with ICI that was in violation of his regulatory and fiduciary duties--a benefit that could have inured to Cascade through its formation of a service corporation. The Director concludes that Simpson was unjustly enriched in connection with this violation and practice. The Director finds that restitution is appropriate under 12 U.S.C. § 1818(b)(6)(A)(i).

Further, the Director concludes that Simpson's insurance operations meet the reckless disregard standard. He acted purposefully, not accidentally, in conducting these operations with Cascade

employees continuously over ten years, which is evidence of clear neglect of OTS regulations and Simpson's fiduciary duty of loyalty. The use of a thrift institution's employees in a business that is run by a director but generates no income for the thrift (and yet for which the thrift pays its employees) presents a danger so obvious that Simpson should have or must have known of it. Simpson's receipt of payments from Worthington in exchange for sending Cascade's business to Worthington was clearly in dereliction of his duty and posed an obvious risk of loss to Cascade. Accordingly, the Director finds that Simpson's insurance business was conducted in reckless disregard for the law and the applicable regulations, and that restitution may be ordered under 12 U.S.C. § 1818(b)(6)(A)(ii).

Simpson, accordingly, is directed to make restitution in the amount of $161,522.

B. Removal and Prohibition Authority

This proceeding involves conduct occurring before and after the enactment of FIRREA. The ALJ erroneously applied the legal standards of the post-FIRREA removal and prohibition statute to all conduct.[31/]

The Director finds, however, that the ALJ's error was immaterial since one of the transactions, the profit-sharing distribution, occurred after the effective

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[31/] Compare 12 U.S.C. § 1818(e) (Supp. II 1990) with 12 U.S.C. § 1464(d)(4) (1988). FIRREA's changes to the legal standards governing the issuance of removal and prohibition orders do not apply to pre-FIRREA conduct. However, FIRREA's expanded remedies (i.e., industry-wide prohibition) may be imposed for pre-FIRREA conduct. In the Matter of O'Keeffe at 13-15.

date of FIRREA and was governed exclusively by the post-FIRREA statute. The Director concludes that the ALJ properly determined that this transaction supported the issuance of an order of prohibition.[32/]

[32/] With regard to this transaction, Simpson breached his fiduciary duties and engaged in an unsafe and unsound practice by directing the distribution; caused a financial loss of $529,500 to Cascade and a financial gain of $105,000 to himself; and was personally dishonest and demonstrated willful disregard for the safety or soundness of the institution. See 12 U.S.C. § 1818(e) (Supp. II 1990).

The Previs transaction occurred prior to the enactment of FIRREA. With regard to this transaction, Simpson violated OTS regulations, breached his fiduciary duties, and engaged in an unsafe and unsound practice; caused a substantial financial loss of $318,424 to Cascade and a financial gain of $20,000 to himself; and was personally dishonest and demonstrated willful and continuing disregard for the safety and soundness of the institution. Accordingly, the Director concludes that Simpson's participation in the Previs loan supports an order of prohibition under the

(continued...)

The ALJ recommended that Simpson be prohibited "from participation in the affairs of Cascade or other Federally regulated banking or savings institution." Under 12 U.S.C § 1818(e)(7), Simpson may be prohibited from participation in many additional institutions and entities. Today's decision prohibits Simpson from participation in the full array of

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32/ (...continued)
requirements set forth in 12 U.S.C. § 1464(d)(4) (1988).

The insurance operations occurred before and after the enactment of FIRREA. With regard to these operations, Simpson violated OTS regulations, breached his fiduciary duties and engaged in an unsafe and unsound practice; caused a substantial loss of $161,522 to Cascade and a financial gain of $161,522 to himself; and was personally dishonest and demonstrated willful and continuing disregard for the safety and soundness of the institution. Accordingly, the Director also concludes that Simpson's participation in the insurance operations supports an order of prohibition under 12 U.S.C. § 1818(e) (Supp. II 1990) and 12 U.S.C. § 1464(d)(4)(A) (1988).

institutions and entities specified under 12 U.S.C. § 1818(e)(7)(A).

C. Civil Money Penalty Analysis

1. Standards Governing the Imposition of CMPs

The Federal Deposit Insurance Act, as amended by FIRREA, employs a three-tiered approach to the assessment of CMPs. 12 U.S.C. § 1818(i)(2). The statute provides for maximum daily CMPs of up to $5,000, $25,000 or $1 million per day, based on the type of conduct involved and the nature and consequences of the violations.

In this proceeding, Enforcement sought a tier-three CMP against the Respondent under 12 U.S.C. § 1818(i)(2)(C). This statute authorizes the imposition of CMPs of up to $1 million per day if the Respondent: (1) knowingly commits any violation of a law or

regulation, engages in an unsafe or unsound practice, or breaches any fiduciary duty; and (2) knowingly or recklessly causes a substantial loss to the association or a substantial pecuniary gain or other benefit to the institution-affiliated party by reason of the violation, practice or breach.

In determining the amount of the CMP imposed, the agency is required to take into account: (1) the size of the financial resources and good faith of the insured depository institution or other person charged; (2) the gravity of the violations; (3) the history of previous violations; and (4) such other matters as justice may require. 12 U.S.C. § 1818(i)(2)(G).

2. Review of the Recommended CMP Amount

An agency record for CMPs must "evince a thorough evaluation of all factors which under the statute must enter into a penalty . . . ." Bullion v. FDIC, 881 F.2d 1368, 1379 (5th Cir. 1989).[33/] The civil money penalty provisions of the FDIC specifically require consideration of four enumerated mitigating factors, including the size of financial resources

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[33/] Bullion was decided under the pre-FIRREA CMP provisions at 12 U.S.C. § 1828(j)(4) (1982) which required consideration of the same statutory mitigating factors at issue here. In Bullion, the court found that, with respect to one of the three respondents, the FDIC "did not deal adequately with the statutory factor of ability to pay." Bullion, 881 F.2d at 1379. On appeal following a second FDIC decision on remand, the court found that the FDIC failed to meet its burden of going forward with evidence on the statutory mitigating factor of ability to pay, and again remanded the decision for further proceedings. Dazzio v. FDIC, 970 F.2d 71 (5th Cir. 1992).

of Respondent. 12 U.S.C. § 1818(i)(2)(G). The factual record in this proceeding has not been sufficiently developed to permit the Director, on review, to determine whether Respondent's financial resources permit the amount of the CMP recommended by the ALJ.

Enforcement has the burden of producing evidence on financial resources, although it need not bear "full responsibility for proving the financial condition" of the respondent, Stanley v. Board of Governors of the Federal Reserve System, 940 F.2d 267, 274 (7th Cir. 1991). The record before the Director is, however, devoid of evidence concerning Simpson's financial resources. Thus, the Director cannot ascertain how substantial an impact the recommended CMP of $138,013

would have on him.[24] Accordingly, the Notice of Assessment is dismissed by the Order accompanying this Decision.

V. CONCLUSION

For the reasons set forth herein, the Director concludes that the following remedies are appropriate: a cease and desist order directing Respondent to make restitution in the total amount of

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[24] Enforcement did not propose, and the ALJ did not recommend, findings of fact regarding Simpson's financial resources, and the record does not contain financial statements for Respondent. The record does refer to one significant asset owned by the Respondent. In connection with the Temporary Cease and Desist Order, Simpson posted approximately $950,000 as security. The Director notes that neither Enforcement nor the ALJ made any attempt to tie this asset to the mitigating factors. Moreover, this amount was posted as security for any restitution that Simpson might be required to pay. Because the amount of the restitution ordered today exceeds the available security, the information on this asset provides little assistance in the determination of the ability to pay a substantial civil money penalty.

$1,009,446 to Cascade; and a prohibition order precluding the Respondent from participation in the conduct of the affairs of Cascade and any institution or entity listed in 12 U.S.C. § 1818(e)(7)(A). The Director further concludes that the failure of Enforcement to provide evidence of all mitigating factors governing the imposition of CMPs requires the dismissal of the CMP assessment sought in the Notice.

ORDER

Upon consideration of the entire record in this matter, including the Recommended Decision of the Administrative Law Judge and the Exceptions to the Recommended Decision filed by both parties, and for the reasons set forth in the above Decision:

The Director of the OTS, pursuant to his authority under 12 U.S.C. § 1818(b) and 12 U.S.C. § 1464(d)(2)(1982) finds that: Jess T. Simpson, in his former capacity as President and Chairman of the Board of Cascade Savings Bank of Everett, Washington, violated OTS regulations including 12 C.F.R. §§ 563.33 and 563.40, and engaged in unsafe or unsound practices and breaches of his fiduciary duty, including those defined in 12 C.F.R. §§ 571.7 and 571.9, in conducting the business of Cascade. The Respondent was unjustly enriched in connection with these violations and practices, and the violations and practices involved reckless disregard for the law and applicable regulations. Accordingly, grounds exist under 12 U.S.C. § 1818(b) to issue a cease and desist order requiring affirmative

action to correct or remedy conditions resulting from these violations and practices.

The Director, pursuant to his authority under 12 U.S.C. § 1818(e), finds that: Simpson, in his capacity specified above, after August 9, 1989, violated OTS regulations including 12 C.F.R. § 563.33, engaged and participated in unsafe and unsound practices in connection with Cascade, and committed and engaged in acts, omissions and practices that constitute breaches of his fiduciary duties to Cascade, including those defined in 12 C.F.R. §§ 571.7 and 571.9. By reason of these violations, practices and breaches Cascade has suffered financial loss and Simpson has received a financial gain and other benefit. The violations, practices and breaches involved personal

dishonesty on the part of Simpson and demonstrated willful and continuing disregard for the safety and soundness of Cascade. Accordingly, grounds exist under 12 U.S.C. § 1818(e) to issue an order prohibiting Simpson from further participation in the conduct of the affairs of Cascade and other institutions and entities listed at 12 U.S.C. § 1818(e)(7).

The Director, pursuant to his authority under 12 U.S.C. § 1464(d)(4)(A) (1982), finds that: Simpson, in his capacity specified above, prior to August 9, 1989, violated OTS regulation including 12 C.F.R. §§ 563.33 and 563.40, engaged and participate in unsafe and unsound practices in connection with Cascade, and committed and engaged in acts, omissions and practices that

constitute breaches of his fiduciary duties to Cascade, including those defined in 12 C.F.R. §§ 571.7 and 571.9. By reason of these violations, practices and breaches Cascade has suffered substantial financial loss and Simpson has received a financial gain. The violations, practices and breaches involved personal dishonesty on the part of Simpson and willful and continuing disregard for the safety and soundness of Cascade. Accordingly, grounds exist under 12 U.S.C. § 1464(d)(4)(A) (1982) to issue an order prohibiting Simpson from further participation in the conduct of the affairs of Cascade and other institutions and entities listed at 12 U.S.C. § 1818(e)(7).

THEREFORE, IT IS HEREBY ORDERED THAT:

1. Respondent, Jess T. Simpson, shall cease and desist from engaging in any act, omission, or practice involving: unsafe or unsound practices; breaches of fiduciary duty as described in 12 C.F.R. §§ 571.7 and 571.9 or successor statutes and regulations, and as established by common law; and violations of 12 C.F.R. §§ 563.33 and 563.40;

2. Within ten (10) business days after the effective date of this Order, Respondent shall pay restitution to Cascade Savings Bank in the amount of One Million Nine Thousand Four Hundred and Forty Six Dollars ($1,009,446), which amount represents restitution, reimbursement, indemnification, or guarantee against loss necessary to correct the conditions resulting from

Simpson's violations and practices. Restitution must be paid in cash, unless payment in another form is approved by the Assistant Regional Director of the Office of Thrift Supervision, Seattle Area Office.

3. Respondent's failure to pay the full amount of the restitution ordered under paragraph 2 will result in the application of the security posted under the temporary cease and desist order issued February 12, 1991, to the extent necessary to satisfy the restitution order.

4. Simpson is prohibited from further participation, in any manner, in the conduct of the affairs of Cascade or any of its subsidiaries pursuant to 12 U.S.C. § 1818(e);

5. While this Order is in effect, Simpson may not continue or commence to hold any office in, or participate in any manner in the conduct of the affairs of, any institution or entity listed in 12 U.S.C. § 1818(e)(7)(A);

6. Conduct prohibited by this order includes the conduct specified under 12 U.S.C. § 1818(e)(6);

7. This Order is subject to the provisions of 12 U.S.C. § 1818(j);

8. To the extent that the Notice of Assessment dated February 12, 1991 assesses civil money penalties, the Notice is dismissed; and

9. The provisions of this Order are effective upon the expiration of thirty (30) days after service of this Order upon Simpson and shall remain effective and enforceable, except to the extent that,

and until such time as, any provisions of this Order shall have been stayed, modified, terminated, or set aside by the Director or a reviewing court, or in accordance with 12 U.S.C. § 1818(e)(7)(B).

THE OFFICE OF THRIFT SUPERVISION

By: /s/ Timothy Ryan
Timothy Ryan
Director

Dated: 11/18/92

157320.2

APPENDIX D

UNITED STATES OF AMERICA
Before the
OFFICE OF THRIFT SUPERVISION

In the Matter of	)	Re: OTS AP 91-6
	)	Dated:
	)	February 12, 1991
JESS T. SIMPSON,	)	
Former President and	)	OTS Order No.
Chairman of the	)	AP 92-123
Board of Directors	)	Dated:
	)	November 18, 1992
Cascade Savings Bank	)	
Everett, Washington,	)	OTS Order No.
	)	AP 93-1
	)	Dated:
	)	January 4, 1993

ORDER

By Final Decision and Order issued November 18, 1992 (OTS Order No. AP 92-123), the Director of the Office of Thrift Supervision issued a Cease and Desist Order requiring, among other things, the Respondent Jess T. Simpson ("Simpson" or

the "Respondent") to pay restitution to Cascade Savings Bank of Everett, Washington ("Cascade" or the "Association") in the amount of $1,009,446. The amount of the restitutio n included $105,000 improperly paid to Simpson in December 1989 under the Association's profit sharing plan.

By letter to the Director dated November 24, 1992 (Appendix A attached hereto), the Respondent asserted that he did not receive the profit sharing paymen t in cash. Rather, on December 31, 1989, the $105,000 profit sharing distribution was credited to Simpson's deferred compensation account with the Association. Respondent represents that, after the close of the evidentiary hearing, Cascade's Board of Directors reversed the distribution to Simpson and removed the

$105,000 credit to Respondent's deferred compensation account. Because the Final Decision and Order did not take this involuntary repayment into account, Simpson argues that he will be required to make an unintended double payment of $105,000. Simpson requests that the Final Decision and Order be modified to clarify this point.

By letters dated November 25, 1992 and December 4, 1992, attached hereto as Appendix B and Appendix C, respectively, both Cascade and OTS Enforcement Counsel concurred in Simpson's representations and interposed no objection to the OTS's recognition of Cascade's revocation of Simpson's profit sharing distribution as partial satisfaction of the restitution that Simpson owes to Cascade.

The Final Decision and Order at page 41, paragraph 2, provides that "restitution must be paid in cash, unless payment in another form is approved by the Assistant Regional Director of the Office of Thrift Supervision, Seattle Area Office." The Acting Director finds that the removal of a credit in the amount of $105,000 from the deferred compensation account is equivalent to payment in cash. Accordingly, the Acting Director interprets the language quoted to authorize payment in the form of Cascade's removal of the credit to Simpson's deferred compensation account.

The Acting Director notes, however, that Simpson has not consented to Cascade's reversal of the $105,000 distribution. Unless Simpson gives such consent, the possibility remains that he

may later dispute Cascade's removal of the credit in a collateral action initiated in another forum. Therefore, the Acting Director will recognize Cascade's reversal of Simpson's profit-sharing distribution as restitution only if Simpson consents to Cascade's removal of the $105,000 credit to his deferred compensation account. By consenting to Cascade's removal of the credit, Simpson does not waive his right to seek judicial review of the merits of the Final Decision and Order under 12 U.S.C. § 1818(h)(2).

Today's Order does not affect the Respondent's obligation to make full restitution in the total amount of $1,009,446 within the time periods set forth in the Director's Final Decision and Order.

THEREFORE, IT IS HEREBY ORDERED THAT:

1. If Simpson consents to Cascade's reversal of the December 1989 profit sharing distribution to Simpson and to it s removal of a credit in the amount of $105,000 from his deferred compensation account, then Simpson shall be deemed to have made restitution in the amount of $105,000 to Cascade in partial satisfaction of the total amount of restitution Simpson owes to Cascade under the Final Decision and Order issued in this proceeding on November 18, 1992.

2. Simpson shall file his consent with the Assistant Regional Director of the Office of Thrift Supervision, Seattle Area Office. The consent shall be in writing, in a form acceptable to the Assistant Regional Director, and shall be filed within ten business days after the

effective date of the Final Decision and Order. Copies of Simpson's consent shall be served on Margaret Hill, Acting Secretary, Office of Thrift Supervision, 1700 G Street, N.W., Washington D.C. 20552 and on Enforcement Counsel.

3. Simpson's written consent described herein shall no be deemed a waiver of his right to seek judicial review of the Final Decision and Order under 12 U.S.C. § 1818(h)(2).

4. Respondent's obligation to pay the restitution required under the Final Decision and Order within the times specified by that Order is not affected by today's Order. Any successful challenge, claim or action by Simpson against Cascade for Cascade's debit to Respondent's deferred compensation account in the amount of $105,000 shall not relieve

Simpson of his obligation to make restitution to Cascade in the full amount ordered pursuant to the Final Decision and Order.

5. The provisions of this Order are effective upon the date of service upon the parties.

Dated: 1/4/93

THE OFFICE OF THRIFT SUPERVISION

By /s/ Jonathan L. Fiechter
Jonathan L. Fiechter
Acting Director

157548.2

APPENDIX E

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

JESS T. SIMPSON, former President and Chairman of the Board of Directors, Cascade Savings Bank, Everett, Washington, Petitioner, v. OFFICE OF THRIFT SUPERVISION, Respondent.	Nos. 92-70797 93-70050 OTS AP 91-6 Order No. AP 92-123 ORDER

Petition for Review of a Decision of the Office of Thrift Supervision

Before: HUG, HALL, and THOMPSON, Circuit Judges.

The panel, as constituted in the above case, has voted to deny petitioner's

petition for rehearing and to reject the suggestion for rehearing en banc.

The full court has been advised of the en banc suggestion and no active judge of the court has requested a vote on whether to rehear the matter en banc. Fed. R. App. P. 35(b).

The petition for rehearing is **DENIED** and the suggestion for rehearing en banc is **REJECTED**.

157545.2

APPENDIX F

UNITED STATES OF AMERICA
Before the
OFFICE OF THRIFT SUPERVISION
DEPARTMENT OF THE TREASURY

In the matter of JESS T. SIMPSON, Former President and Chairman of the Board of Directors Cascade Savings Bank Everett, Washington	**Re: OTS AP 91-6** **Dated:** **February 12, 1991**

NOTICE OF CHARGES AND HEARING FOR AN ORDER TO CEASE AND DESIST AND TO DIRECT RESTITUTION AND OTHER AFFIRMATIVE CORRECTIVE RELIEF, NOTICE OF INTENTION TO PROHIBIT, AND NOTICE OF ASSESSMENT OF CIVIL MONEY PENALTY

In accordance with the provisions of Sections 8(b) and 8(e) of the Federal Deposit Insurance Act ("FDIA"), as amended by the Financial Institutions Reform,

Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183, 450-464 ("FIRREA"), 12 U.S.C. §§ 1818(b) and (e), and Sections 407(e) and (g) of the National Housing Act Of 1934, as amended 12 U.S.C. §§ 1730(e) and (g) (1982) ("NHA"), the Office of Thrift Supervision ("OTS"), acting on its own behalf and as successor in interest to the Federal Savings and Loan Insurance Corporation ("FSLIC"), being of the opinion that Jess T. Simpson ("Simpson"), by virtue of his conduct with respect to Cascade Savings Bank, Everett, Washington ("Cascade"), has violated provisions of the Rules and Regulations applicable to All Savings Associations, 12 C.F.R. Part 561, et seq. (1990), has engaged in unsafe or unsound practices in violation of the FDIA and the NHA, and has committed

acts, omissions and practices that constitute willful disregard for Cascade's safety and soundness and breaches of fiduciary duty, that such violations or practices involve personal dishonesty and resulted in losses and damage to Cascade and personal gain to himself, and that such violations or practices involved reckless disregard for law or regulation or resulted in unjust enrichment, and that grounds exist to institute administrative cease and desist proceedings, including a determination of whether the ordering of restitution or other affirmative corrective relief is appropriate, and prohibition proceedings against Simpson, hereby issues this Notice of Charges and Hearing for an order to Cease and Desist and to Direct Restitution and Other

Affirmative Corrective Relief and Notice of Intention to Prohibit.

Further, pursuant to the provisions of Section 8(i) of FDIA, as amended by FIRREA, 12 U.S.C. § 1818(i), OTS, based upon its opinion that Simpson knowingly and recklessly engaged in unsafe or unsound practices and breached his fiduciary duty to Cascade, that such practices and breaches have caused or are likely to cause substantial loss to Cascade, and that Simpson has derived substantial pecuniary gain and other benefits from such violations and unsafe or unsound practices, hereby issues this Notice of Assessment of a Civil Money Penalty against Simpson.

I. JURISDICTION

1. Cascade Savings Bank, Everett, Washington ("Cascade"), is a state-

chartered mutual savings and loan association that maintains its principal place of business in Everett, Washington.

2. Cascade is a "savings association" as defined by Section 2(4) of the HOLA, as amended by Section 301 of the FIRREA, 12 U.S.C. § 1462(4), and Section 3(b) of the FDIA, as amended by Section 204 of the FIRREA, 12 U.S.C. § 1813(b), and is an "insured depository institution" as defined by Section 3(c)(2) of the FDIA, as amended by Section 204 of the FIRREA, 12 U.S.C. § 1813(c)(2).

(a) Until August 9, 1989, the accounts of Cascade were insured by the FSLIC pursuant to Section 403(b) of the NHA, 12 U.S.C. § 1726(b), by reason of which it was an "insured institution" within the meaning of the NHA.

(b) As of August 9, 1989, pursuant to the provisions of FIRREA, the insurance of the accounts of Cascade was transferred to the Federal Deposit Insurance Corporation.

(c) Until August 9, 1989, the Federal Home Loan Bank Board ("Bank Board"), as operating head of the FSLIC, was the regulatory agency with jurisdiction over Cascade and its officials pursuant to Sections 403 and 407 of the NHA, 12 U.S.C. §§ 1726 and 1730.

(d) As of August 9, 1989, pursuant to Section 3(q) of the FDIA, as amended by Section 204 of the FIRREA, 12 U.S.C. § 1813(q), the OTS succeeded to the interests of the FSLIC with respect to the supervision and regulation of all savings associations, and thus became the "appropriate Federal banking agency" with

jurisdiction over Cascade and persons participating in the conduct of the affairs thereof.

(e) The Director of the OTS has the authority to institute administrative proceedings to determine whether a cease and desist order directing restitution and other affirmative corrective relief, prohibition order and order assessing a civil money penalty should issue against Simpson pursuant to Section 5(d)(1)(A) of the HOLA, as amended by Section 301 of the FIRREA, 12 U.S.C. § 1464(d)(1)(A), and Section 8 of the FDIA, as amended by the FIRREA, 12 U.S.C. § 1818.

3. At all times relevant herein, Simpson was an officer, director and person participating in the conduct of the affairs of Cascade and, as such, was an "institution-affiliated party" of Cascade

as that term is defined by Section 3(u) of the FDIA, as amended by Section 204 of the FIRREA, 12 U.S.C. § 1818(u). By virtue of these positions, Simpson is subject to the OTS's authority to maintain cease and desist and prohibition proceedings, including restitution, and assessment of civil money penalties.

II. FACTS

A. Profit Sharing

4. Since 1985, as part of its employee compensation plan, Cascade has maintained an annual profit-sharing plan.

5. Under this plan, a target for net profit before taxes ("NPBT") was established at the beginning of each calendar year by Cascade's Board of Directors, and half of all NPBT realized in excess of the target was distributed to eligible employees of Cascade, generally

managers, at the end of each calendar year.

6. Upon approval by the Compensation Committee of the Board of Directors of Cascade, Simpson was responsible for the distribution of funds under the profit-sharing plan.

7. On or about December 6, 1989, due to concerns about the new regulatory capital requirements of FIRREA and concerns raised by federal regulators about potential asset write-downs to the December 31, 1989 annual financial statements, a majority of the members of the Compensation Committee directed Simpson not to distribute any funds under the profit-sharing plan until completion of the 1989 audit of Cascade.

8. On or about December 20, 1989, Simpson, along with other members of the

Board of Directors and employees of Cascade, attended a meeting wherein Cascade's auditors, Peat Marwick, raised concerns about potential substantial write-downs for, among other things, excess loan servicing fees on the 1989 audited financial statements.

9. On or about December 27, 1989, OTS issued a directive ordering Cascade to recognize $1 million in write-downs for excess loan servicing fees for 1989.

10. This write-down, as well as other write-downs directed by Peat Marwick during its audit of Cascade's 1989 financial statements, completed at the end of March, 1990, reduced Cascade's NPBT to a point where the target for profit-sharing was not met, no pool would have been created, and no funds would have been disbursed.

11. During all of the periods referred to in paragraphs 7-10 above, Cascade had a 2.6% deficiency in risk-based capital.

12. Simpson was on notice of the capital deficiency noted in paragraph 11 because on October 16, 1989, federal regulators had written Cascade's Board of Directors detailing regulatory concerns about insufficient capital.

13. Notwithstanding these admonitions that he not distribute profit-sharing funds until the completion of the audit, on or about December 29, 1989, Simpson willfully caused approximately $530,000 to be distributed under the profit-sharing plan.

14. Of this amount, Simpson received approximately $105,000, which has been

maintained in a deferred compensation account in his name at Cascade.

15. The release of the $530,000, contrary to the specific orders of a majority of the Compensation Committee and in the face of ordered write-downs of $1 million and potential write-downs of greater amounts, constitutes an unsafe and unsound practice and a breach of Simpson's fiduciary duty to Cascade, such practice and breach being compounded by Cascade's deficient capital position.

16. By virtue of the conduct set forth above, Simpson was personally dishonest; acted with willful disregard for Cascade's safety and soundness; willfully, knowingly and recklessly caused substantial loss and damage to Cascade; and realized substantial personal gain and unjust enrichment due to the breach of his

fiduciary duty to Cascade and reckless disregard for its safety and soundness.

17. Simpson breached his fiduciary duty and knowingly engaged in an unsafe and unsound practice by placing his interests before those of Cascade when he caused payment under the profit-sharing plan to be made at a time when he had been directed by a majority of the Compensation Committee not to do so; when Cascade was capital deficient; and when the chances of meeting the 1989 target had become highly unlikely.

B. **The Previs Loan**

18. On or about April 27, 1981, Cascade's Loan Committee, upon the direction of Simpson, made a real estate loan of approximately $250,000 to Randy Previs ("Previs") so that he could purchase a parcel of land known as the

Valley View Ranch, located in Thorp, Washington. The loan was secured by the land and had a three-month maturity date of July 27, 1981.

19. On or about June 19, 1981, Cascade increased the initial loan by approximately $64,000, approximately $13,000 of which was for capitalized interest and fees. The initial loan and the $64,000 extension were consolidated into one loan, with a new three-month maturity date of October 25, 1981. Subsequent thereto, the loan was refinanced on or about October 26, 1981 to include $24,600 in capitalized interest and fees, and the term was extended another 90 days, to January 25, 1982. On or about April 20, 1982, the loan was again refinanced, with an additional advance of $51,900 in capitalized interest

and fees, and the term was extended another 90 days, due on July 15, 1982.

20. On October 31, 1983, the loan to Previs was foreclosed upon by Cascade, resulting in a loss to Cascade of approximately $238,000.

21. Previs had at no time during the life of these loans made any payments of any sort to Cascade, including principal, interest or fees.

22. Although approval of the initial loan was ratified by Cascade's Board of Directors on June 9, 1981, as were the subsequent refinancings, such Board approval was made without the benefit of certain material information about the loans known by Simpson, including but not limited to:

(a) that the loan to Previs to purchase property in eastern Washington

was the only loan Cascade had ever made in that part of the state;

(b) that the loan was made notwithstanding the fact that an outstanding bankruptcy judgment had been issued against Previs in February, 1980;

(c) that negotiations between Simpson and Previs for the purchase by Previs of Simpson's yacht had begun prior to Previs' loan application;

(d) that Previs did in fact purchase Simpson's yacht on or about July 1, 1981 for $180,000;

(e) that Simpson had promised Previs that Simpson would arrange the Valley View Ranch loan for Previs in return for Previs' purchase of Simpson's yacht;

(f) that Simpson was personally involved with the acquisition of the loan

by Previs and had a conflict of interest with respect to it; and

(g) that $50,000 of the proceeds from the June 19, 1981 loan increase to Previs of $64,000 was used to pay for post-sale repairs on the yacht and for commissions owed by Simpson incidental to the sale of the yacht.

23. Simpson breached his fiduciary duty to Cascade and engaged in unsafe and unsound practices by not disclosing to Cascade's Loan Committee and its Board of Directors any one or all of the details discussed in paragraph 22 above. These disclosures were necessary for the Loan Committee and the Board of Directors to make an informed decision regarding this series of loans.

24. Simpson breached his fiduciary duty to Cascade, engaged in unsafe and

unsound practices, and acted contrary to the applicable conflict of interest policy statement set forth at 12 C.F.R. § 571.7, when he put his undisclosed personal interest in selling his yacht ahead of the interests of Cascade.

25. Simpson breached his fiduciary duty and engaged in unsafe and unsound practices, and engaged in a practice amounting to an improper conflict of interest by causing Cascade to enter into the Previs loan transactions when the loans were based in whole or in part on the undisclosed sale of his yacht to Previs.

26. Simpson's receipt of anything of value, including the proceeds of the sale of his yacht, in connection with loans by Cascade to Previs, is a violation of 12 C.F.R. § 563.40, "Restrictions on Loan

Procurement Fees, Kickbacks and Unearned Fees," is an unsafe and unsound practice and a breach of Simpson's fiduciary duty to Cascade.

28. Simpson caused substantial loss and other damage to Cascade and realized personal gain by reason of his engaging in the foregoing regulatory violations, unsafe and unsound practices, and breaches of fiduciary duty. These acts also constituted personal dishonesty and willful and continuing disregard for Cascade's safety and soundness by Simpson. These acts further constituted unjust enrichment to Simpson and amount to reckless disregard for the law.

C. Insurance Commerce, Inc.

29. From on or about January 1, 1981 through May 10, 1990, Insurance Commerce, Inc. ("ICI"), a company incorporated in

the state of Washington and maintaining the same mailing address as that of Cascade, was controlled by Simpson. During this period, ICI collected at least $161,000 in income from Family Life Insurance Company of Seattle, Washington, and Worthington Insurance Company of Bothell, Washington. Of this amount, approximately $13,013 was received by ICI after August 9, 1989.

30. This income was generated as a result of contractual arrangements between Cascade and/or ICI and the insurance companies. Details regarding these arrangements were negotiated by Simpson and representatives of the insurance companies.

31. The arrangements, in part, required Cascade to provide to the insurance companies the names of persons

who had secured residential mortgage loans from Cascade. The insurance companies then solicited these Cascade customers in an attempt to sell insurance policies, including mortgage life insurance in the case of Family Life Insurance Company. A substantial number of policies were sold to Cascade's customers in this manner.

32. One of these arrangements required Cascade, upon receipt of monthly mortgage payments, including insurance premiums, to remit the premium payment to Family Life Insurance Company. Under another arrangement, Cascade acquired its own insurance, including property liability, commercial, blanket bond, employee and officer liability, and automobile insurance, from Worthington Insurance Company.

33. Most, if not all, of the work performed on behalf of ICI in connection with these arrangements was done by Cascade employees and on Cascade time.

34. Simpson, in connection with receipt of moneys by ICI, derived personal benefit from the receipt of this money, often loaning portions of the money to his children.

35. ICI was maintained for the primary purpose of receiving moneys paid under these arrangements and served as a depository for these moneys.

36. During all relevant times herein, Cascade could have formed a subsidiary to receive the fees otherwise paid to ICI for work performed by employees of Cascade.

37. The cost to Cascade of forming a subsidiary to perform this function would

have been minimal, particularly since all of the work for which ICI received fees was already being performed by Cascade employees.

38. During all relevant times herein, Simpson did not disclose material facts about ICI's business and his relationship thereto to the Board of Directors of Cascade, including but not limited to:

(a) his control of ICI;

(b) the use of Cascade employees in furtherance of ICI's business;

(c) income earned by ICI from the arrangements described in paragraphs 31-33 above; and

(d) loans by ICI to Simpson's relatives and/or friends.

39. The arrangements between ICI and the insurance companies constitutes a usurpation of a corporate opportunity of Cascade and, as such, was contrary to the policy statement set forth at 12 C.F.R. § 571.9.

40. Under 12 C.F.R. § 571.9, such a usurpation constitutes an unsafe and unsound practice, and Cascade is entitled to all profits attributable to the usurpation.

41. Such a usurpation also constitutes a breach of Simpson's fiduciary duty to Cascade, and evidences Simpson's personal dishonesty and willful and continuing disregard for the safety and soundness of Cascade.

42. The uncompensated performance of work by Cascade employees for ICI and/or Simpson during the hours of their

employment by Cascade also amounts to a violation of 12 C.F.R. § 563.33(b). The receipt of moneys generated by using Cascade employees in violation of 12 C.F.R. § 563.33(b) also amounts to a breach of Simpson's fiduciary duty to Cascade and an unsafe and unsound practice, and evidences Simpson's personal dishonesty and willful and continuing disregard for the safety and soundness of Cascade.

43. Simpson caused financial loss and other damage to Cascade and realized pecuniary gain or other benefit by reason of his engaging in the foregoing regulatory violations, recklessly engaging in the foregoing unsafe and unsound practices and breaching his fiduciary duty to Cascade. These acts also constituted personal dishonesty and willful and

continuing disregard for Cascade's safety and soundness by Simpson.

D. **Personal Educational Expenses**

44. From at least on or about January 1, 1987 through at least January 23, 1990, Simpson caused Cascade to incur costs of at least $4,500, purportedly representing Cascade business expenses incurred, directly or indirectly, by Simpson. In fact, such expenses had no legitimate business purpose, but represented payments for the education of Simpson's wife and son, neither of whom were employed by Cascade when the expenses were incurred. These items were personal expenses of Simpson, and accordingly, should not have been paid by Cascade. Of this amount, approximately $1300 was paid by Cascade after August 9, 1989.

45. Cascade's payment of these expenses constitutes a financial gain or benefit to Simpson of at least $4,500, and corresponding loss and damage to Cascade.

46. Cascade's payment of expenses unrelated to the business of Cascade is an unsafe and unsound practice, constitutes a breach of Simpson's fiduciary duty and evidences Simpson's personal dishonesty and willful and continuing disregard for the safety and soundness of Cascade.

47. Simpson caused financial loss and other damage to Cascade and realized pecuniary gain, unjust enrichment, or other benefit by reason of his engaging in the foregoing regulatory violations, recklessly engaging in the foregoing unsafe or unsound practices, and breaching his fiduciary duty to Cascade. These acts also constituted personal dishonesty,

willful and continuing disregard for Cascade's safety and soundness, and reckless disregard for the law by Simpson.

III. GROUNDS FOR ISSUANCE OF ORDERS TO CEASE AND DESIST, AND TO DIRECT RESTITUTION AND OF PROHIBITION

48. Based on the foregoing facts, the following grounds exist for the issuance of orders to cease and desist, including the ordering of restitution and other affirmative corrective action, and of prohibition against Jess T. Simpson:

a. Simpson has violated regulations, engaged and participated in unsafe and unsound practices in conducting the business of Cascade, and has committed and engaged in acts, omissions and practices which constitute breaches of his fiduciary duty; and

b. By reason of the foregoing violations, practices and breaches,

Cascade has suffered financial loss and other damage, the interests of Cascade's depositors has been or could be prejudiced, and Simpson has received financial gain and other benefit; and

c. The foregoing violations, practices and breaches involve personal dishonesty by Simpson and his willful and continuing disregard for Cascade's safety and soundness; and

d. The foregoing violations, practices and breaches resulted in unjust enrichment to Simpson and involve his reckless disregard for the law.

IV. NOTICE OF HEARING TO DETERMINE WHETHER ORDERS TO CEASE AND DESIST (INCLUDING DIRECTING RESTITUTION AND OTHER AFFIRMATIVE CORRECTIVE RELIEF), AND PROHIBITION SHOULD ISSUE

Notice is hereby given that pursuant to Sections 407(e) and (g) of the NHA, 12 U.S.C. § 1730(e) and (g), and

Sections 8(b) and (e) of FDIA, as amended by FIRREA, to be codified at 18 U.S.C. § 1818(b) and (e), an administrative hearing will be held to determine whether orders to cease and desist and prohibition should be issued against Simpson. The hearing will also include a determination as to whether Simpson shall be required to take affirmative action to correct the conditions resulting from the practices alleged herein, including restitution, reimbursement, indemnification, guarantees against loss, or such other action as is determined to be appropriate. The hearing will be held within the Federal judicial district for the State of Washington, and is fixed for a date no later than sixty (60) days after issuance of this Notice, subject to change by Order of the Administrative Law Judge assigned to this

hearing or by Order of the Director of OTS. The exact time of day and location for the commencement of the hearing will be announced at a later time. The hearing will be conducted by an Administrative Law Judge in accordance with the adjudicatory provisions of the Administrative Procedure Act, 5 U.S.C. §§ 554-557 (1982), and the Rules of Practice and Procedure of the Office of Thrift Supervision, 12 C.F.R. Part 509 et seq. (1990) ("Rules").

Simpson is hereby directed to file an Answer to this Notice within 20 days from the date of service. The requirements of the Answer, as well as the consequences of failure to file an Answer, are set forth in the Rules.

V. GROUNDS FOR ASSESSMENT OF CIVIL MONEY PENALTY

Based upon the foregoing facts, OTS states that Simpson knowingly and/or recklessly:

a. violated the Rules and Regulations applicable to all Savings Associations at 12 C.F.R. §§ 563.33(b) and 563.40, and failed to comply with the policy statements set forth at 12 C.F.R. §§ 571.7 and 571.9;

b. engaged in unsafe and unsound practices in conducting the affairs of Cascade; or

c. breached his fiduciary duty to Cascade; and

d. caused a substantial loss to Cascade and received a substantial pecuniary gain, and other benefit by reason of such violations, unsafe and

sound practices or breaches of his fiduciary duty.

VI. NOTICE OF ASSESSMENT OF CIVIL MONEY PENALTY

Based upon the foregoing conduct, Notice is hereby given that the OTS assesses a civil money penalty against Simpson for $134,313, pursuant to Section 8(i) of the FDIA, as amended by FIRREA, 12 U.S.C. § 1818(i).

This assessment is issued on the basis of the above-mentioned violations taking into account the losses to the United States, the size of financial resources, and the presence or absence of good faith of Simpson, the gravity of the violations, and the history of previous violations, as required by Section 8(i) of the FDIA, as amended by FIRREA, 12 U.S.C. § 1818(i)(2)(G).

Simpson's remittance of this penalty should be payable to the Treasurer of the United States and delivered to:

Deputy Chief Counsel for
Enforcement
Office of Thrift Supervision
U.S. Treasury Department
1700 G Street, N.W.
Washington, D.C. 20552

Pursuant to Section 8(i) of the FDIA, as amended by FIRREA, 12 U.S.C. § 1818(i)(2)(H), Simpson is hereby afforded the opportunity for a hearing before the OTS concerning this assessment, based upon a request for a hearing made by Simpson within twenty (20) days after the issuance and service of this Notice, which hearing shall be conducted pursuant to 12 C.F.R. § 509 et seq. (1990).

If a timely request by Simpson is made for such a hearing, then any such hearing as it relates to assessments shall be consolidated with the hearing provided

for in Section IV. Any such hearings shall be conducted pursuant to 12 C.F.R. Part 509, et seq. (1990), which requires, among other things, the filing of an Answer to this Notice of Assessment. If Simpson fails to request such a hearing within the above twenty (20) day period, the assessment against such party shall constitute a final and unappealable Order.

/s/ Timothy Ryan
Timothy Ryan
Director

157428.2

APPENDIX G

CASCADE SAVINGS BANK, a Washington mutual savings and loan association, Plaintiff, v. JESS T. SIMPSON, Defendant.	NO. _____ COMPLAINT

Plaintiff brings the following claims against defendant:

1. Cascade Savings Bank ("Cascade") is a Washington mutual savings and loan association chartered under Title 33 RCW. Cascade's principal place of business is Everett, Washington.

2. As a "savings association" whose deposit accounts are insured by the Federal Deposit Insurance Corporation, Cascade is an "insured depository institution" within the meaning of 12 U.S.C. § 1813(b)(1)(B) and (c)(2), regulated by, among others, the federal Office of Thrift Supervision ("OTS"). 12 C.F.R. §§ 500.1, 500.4. See also 12 C.F.R. § 508.2(e) (as used in 12 C.F.R. Part 500, "association" means "savings association" as defined in 12 U.S.C. § 1813).

3. Jess T. Simpson ("Simpson") is an individual residing in Mill Creek, Washington. He is the former president and former Chairman of the Board of Directors of Cascade.

4. Simpson was at all relevant times an "affiliated person" of Cascade, as defined in 12 C.F.R. § 561.5.

5. Insurance Commerce, Inc. ("ICI") is a corporation organized under the laws of the State of Washington. During the time relevant to this lawsuit, ICI (and any predecessor or successor corporation) was "owned" by Simpson, as that term is defined in 12 C.F.R. § 556.16(a)(1), 12 C.F.R. § 556.16(a)(1)(ii) or 12 C.F.R. § 556.16(a)(1)(iii). ICI was also an "affiliate" of Cascade, as that term is used in 12 C.F.R. § 561.4(c); and ICI was an "affiliated person" of Cascade, as that term is defined in 12 C.F.R. § 561.5(d)(1).

6. During the time relevant to this lawsuit, Simpson was an officer and director of Cascade, and as such, he owed

Cascade a statutory fiduciary obligation to discharge his duties in good faith and with the diligence, care and skill that an ordinary, prudent person would exercise under similar circumstances. RCW 33.16.060.

EXPENSES

7. Between 1981 and 1990, Simpson claimed reimbursement or had Cascade pay for more than $130,000 of expenses he alleged were business expenses, but that were in actuality personal expenses.

8. The expenses identified in paragraph 6 either were not authorized by the Board of Directors of Cascade or were authorized pursuant to an erroneous belief that the expenses were business expenses.

9. Simpson should not have been reimbursed for or charged to Cascade the expenses referenced in paragraph 7.

10. Simpson's claim for reimbursement or payment by Cascade of the expenses referenced in paragraph 7 constituted a breach of his fiduciary duty to Cascade.

COUNT I

11. Cascade reasserts the allegations contained in paragraphs 1 through 10.

12. Simpson's improper submission of expenses described in paragraph 7, which constitute a breach of his fiduciary duty to Cascade, entitles Cascade to restitution of those expenses plus interest thereon.

COUNT II

13. Cascade reasserts the allegations contained in paragraphs 1 through 10.

14. Simpson's improper submission of the expenses described in paragraph 7 constituted an improper direct or indirect interest in Cascade's profits, which resulted in his receipt of more than his authorized compensation in violation of RCW 33.16.030(1).

15. Cascade is entitled to restitution of the excess compensation plus interest on those amounts.

COUNT III

16. Cascade realleges the allegations contained in paragraphs 1 through 10.

17. Simpson's actions with regard to the expenses described in paragraph 7 constitute conversion of Cascade's profits.

18. Cascade is entitled to restitution of those converted profits plus interest.

COUNT IV

19. Cascade realleges the allegations contained in paragraphs 1 through 10.

20. Simpson's claims regarding the expenses described in paragraph 7 violated his employment agreement with Cascade.

21. Cascade is entitled to damages for Simpson's breach of contract, measured by the unproperly claimed expenses plus interest.

COUNT V

22. Cascade realleges the allegations contained in paragraphs 1 through 10.

23. Simpson's claims regarding the expenses described in paragraph 7 constituted misrepresentation.

24. Cascade is entitled to recover the amount of the improperly claimed expenses plus interest because of that misrepresentation.

COUNT VI

25. Cascade realleges the allegations contained in paragraphs 1 through 10.

26. Simpson's claims regarding the expenses described in paragraph 7 constituted misrepresentation.

27. Cascade is entitled to recover its damages for Simpson's misrepresentations.

INSURANCE COMMERCE, INC.

28. Between January 1, 1981, and March 5, 1990, ICI was engaged, primarily

in the business of referring insurance coverage and sharing commissions therefor. Among the sources of revenue for ICI during that time were (1) commissions from insurance policies placed for and on behalf of customers of Cascade, and (2) commissions from insurance coverage placed for Cascade itself.

29. Between January 1, 1981, and March 5, 1990, ICI had net revenues as a result of the income described in paragraph 28 of approximately $197,000.

30. Between January 1, 1981, and March 5, 1990, ICI's expenses were essentially borne by or charged to Cascade.

31. Between January 1, 1981, and March 5, 1990, Simpson owned or controlled ICI, either directly through his nominee, his daughter Laelanne Lee, or through

Financial Commerce, Inc., ("FCI"). During this time Simpson also treated ICI as a personal asset.

32. Between January 1, 1981, and March 5, 1990, Cascade could have engaged directly or indirectly (through a service corporation) in the business in which ICI engaged.

33. The income earned by ICI constituted a usurpation of a business opportunity of Cascade by Simpson in violation of state law.

34. Simpson's ownership or management and control of ICI, while an officer and director of Cascade or while ICI usurped a business opportunity of Cascade, constituted a breach of Simpson's fiduciary duty to Cascade.

COUNT VII

35. Cascade realleges the allegations set forth in paragraphs 1 through 5 and paragraphs 28 through 34.

36. The actions of Simpson in forming and operating ICI and dealing with Cascade and its customers constituted usurpation of Cascade's corporate opportunity to engage in the insurance business in violation of federal regulation 12 C.F.R. § 556.16(b).

37. Because of Simpson's usurpation of Cascade's corporate opportunity, Cascade is entitled to recover the profits of ICI during the period of usurpation. 12 C.F.R. § 556.16(e).

COUNT VIII

38. Cascade realleges the allegations set forth in paragraphs 1 through 5 and paragraphs 28 through 34.

39. The opportunity to engage in the insurance agency business was within Cascade's powers and was a present or potential practical advantage to Cascade. Simpson's taking advantage of the business opportunity for his own direct or indirect personal benefit was a breach of his federal fiduciary duty to Cascade. 12 C.F.R. § 571.9(a).

40. Cascade is entitled to recover the profits of ICI attributable to Simpson's breach of fiduciary duty. 12 C.F.R. 571.9(b); 12 C.F.R. § 556.16(e).

COUNT IX

41. Cascade realleges the allegations set forth in paragraphs 1 through 5 and paragraphs 28 through 34.

42. Simpson's ownership or management and control of ICI while an officer and director of Cascade

constituted a violation of his duty to avoid a conflict of interest or the appearance of a conflict of interest between his personal financial interest and the interests of Cascade. 12 C.F.R. § 571.7(b).

43. Cascade is entitled to recover the profits of ICI attributable to Simpson's improper conflict of interest. 12 C.F.R. § 571.9(b); 12 C.F.R. § 556.16(e).

COUNT X

44. Cascade realleges the allegations set forth in paragraphs 1 through 5 and paragraphs 28 through 34.

45. Simpson's ownership or control of ICI and generation of income on behalf of ICI while Simpson was an officer and director of Cascade or while ICI usurped a business opportunity of Cascade

constituted a breach of Simpson's state law fiduciary duty. RCW 33.16.060.

46. As a result of Simpson's breach of fiduciary duty, Cascade is entitled to recover as damages the amount of income earned by ICI between January 1, 1981, and March 5, 1990, plus interest.

COUNT XI

47. Cascade realleges the allegations set forth in paragraphs 1 through 5 and paragraphs 28 through 34.

48. The income earned by ICI between January 1, 1981, and March 5, 1990, constitutes an improper direct or indirect interest of Simpson in the gains or profits of Cascade in excess of his authorized compensation. RCW 33.16.030(1).

49. Cascade is entitled to recover from Simpson the improper interests in its

gains and profits, measured by the income earned by ICI, plus interest.

COUNT XII

50. Cascade realleges the allegations set forth in paragraphs 1 through 5 and paragraphs 28 through 34.

51. ICI obtained loans from Cascade between January 1, 1981, and March 5, 1990, which bore interest at a rate less than the rate charged to nonaffiliated borrowers. Simpson obtained those loans for and as agent of ICI.

52. Simpson's actions in obtaining loans as agent for ICI violated Washington proscriptions on loans for the direct or indirect benefit of directors. RCW 33.16.030(3).

53. Cascade is entitled to recover damages as a result of those loans, plus interest.

COUNT XIII

54. Cascade realleges the allegations set forth in paragraphs 1 through 5 and paragraphs 28 through 34.

55. The loans Simpson obtained on behalf of ICI violated the regulations governing loans by Cascade to affiliated person contained in 12 C.F.R. § 563.43(b)(5).

56. Cascade is entitled to recover damages from Simpson for those improper loans.

COUNT XIV

57. Cascade realleges the allegations set forth in paragraphs 1 through 5 and paragraphs 28 through 34.

58. Simpson had Cascade employees perform ICI work during Cascade bank hours. Those employees were not reimbursed by ICI and Cascade was not

reimbursed for the use of their time on behalf of ICI.

59. Simpson's actions in having ICI work performed by Cascade employees constituted improper employment of a salaried officer or employee by an affiliated person, a breach of his fiduciary duties and violation of regulations requiring him to avoid conflicts of interest on the appearance thereof. 12 C.F.R. § 563.33(b).

60. Cascade is entitled to recover damages incurred by it as a result of Simpson's use or employment of Cascade employees to perform ICI work during Cascade's business hours.

PREVIS LOAN

61. In 1981, Simpson facilitated a loan by Cascade to Katie L. Previs Land Company, Inc. That loan was ostensibly to

finance the purchase of the Valley View Ranch in Thorpe, Washington.

62. The purchase of the Valley View Ranch closed in May 1981.

63. An advance on the loan to Katie L. Previs Land Company, Inc., was made on June 19, 1981, in the amount of $51,196. This advance was ostensibly part of the loan for the purchase of the real estate.

64. At the same time that Katie L. Previs Land Company, Inc., was purchasing Valley View Ranch, Randy Previs agreed to purchase from Simpson his personal yacht, the M.Y. Laelanne. Previs's purchase of the vessel from Simpson closed on July 1, 1981.

65. The June 19, 1981, advance of $51,196 was in fact for the purpose of benefiting Simpson in the sale of his boat to Previs. At Simpson's direction,

approximately $30,000 of that advance was directed for repairs to the M.Y. Laelanne prior to the sale to Previs, and the other $20,000 was directed for the broker commission for which Simpson was obligated.

66. To Simpson's knowledge, purpose of the loan was in fact to help finance the purchase of the M.Y. Laelanne. This purpose was not disclosed by Simpson.

67. Cascade ultimately lost approximately $238,000 on the Previs loan.

COUNT XV

68. Cascade realleges the allegations set forth in paragraphs 1 through 5 and the paragraphs 61 through 67.

69. Simpson's actions in tying the sale of his boat to the loan to Previs and not disclosing such constituted a breach

of his fiduciary duty to Cascade. RCW 33.16.060.

70. Cascade is entitled to recover its damages for Simpson's breach of fiduciary duty.

COUNT XVI

71. Cascade realleges the allegations set forth in paragraphs 1 through 5 and the paragraphs 61 through 67.

72. The $51,196 advanced for the boat transaction constituted compensation to Simpson for procuring the loan on behalf of Previs, received in violation of 12 C.F.R. § 563.40(a).

73. Cascade is entitled to recover its damages as a result of Simpson's improper receipt of compensation for the procurement of the loan.

COUNT XVII

74. Cascade realleges the allegations set forth in paragraphs 1 through 5 and the paragraphs 61 through 67.

75. The $51,196 paid for the benefit of Simpson from the proceeds of the Previs loan constituted a kickback to Simpson for assisting in the procurement of the loan for Previs.

76. The receipt of a kickback by Simpson for the procurement of the loan was illegal. 12 C.F.R. § 563.40(b).

77. Cascade is entitled to recover its damages for Simpson's improper receipt of a kickback.

COUNT XVIII

78. Cascade realleges the allegations set forth in paragraphs 1

through 5 and the paragraphs 61 through 67.

79. Simpson directed or allowed the purpose of the Previs loan to be listed in Cascade's records as a real estate loan, when he knew it was, in fact, also a boat loan in which he had personal interest. Simpson also directed disbursement of the advance for the boat transaction.

80. Simpson's direction or allowance of the misstatement and his participation in the partial disbursement of loan proceeds for the boat transaction and his receipt of benefit from the proceeds constituted a breach of his fiduciary duty to Cascade. RCW 33.16.060.

81. Simpson's actions with regard to the Previs loan violated the proscription against false statements or false entries

on the books of Cascade set forth in RCW 33.36.040.

82. Based on the foregoing violations of Title 33, Simpson knowingly permitted Previs to borrow funds in violation of Title 33.

83. Simpson became personally liable to Cascade for any loss or damage it sustained as a result of the Previs loan 33.24.200.

84. Cascade is entitled to recover from Simpson all damages it incurred as a result of the Previs loan, including but not limited to principal, interest and costs and fees. RCW 33.24.200.

DEFERRED COMPENSATION

85. Cascade officers were permitted to share in a profit sharing pool as

defined in Cascade's then existing profit sharing plan.

86. Under the plan, the profit sharing pool was created by allocating 50 percent of net profit before taxes above a target level of profit.

87. In 1989, Cascade's preliminary unaudited financial results indicated that profit sharing payments for 1989 could be made at the maximum level. Prior to the time that profit sharing payments were made, however, Cascade's accountants informed Simpson that certain adjustments likely would have to be made which would significantly reduce or totally eliminate the profit sharing pool.

88. Simpson knew or should have known that the payment of maximum profit sharing amounts should have awaited the

final, audited results of Cascade's 1989 financial performance.

89. Nevertheless, Simpson directed payment of the maximum profit sharing amounts before audited results were available. Simpson's share of such amounts was $105,000, which was allocated to his deferred compensation account.

COUNT XIX

90. Cascade realleges the allegations contained in paragraphs 1 through 5 and paragraphs 85 through 89.

91. Any agreement of Cascade and Simpson to pay profit sharing for 1989 was a mutual mistake based on a mistaken belief that a profit sharing pool existed.

92. Cascade is entitled to rescission of the payment and to restitution of the $105,000 and of any interest thereon credited to Simpson's

deferred compensation account, all based on the mutual mistake.

COUNT XX

93. Cascade realleges the allegations contained in paragraphs 1 through 5 and paragraphs 85 through 89.

94. Simpson was unjustly enriched in the amount of $105,000, plus interest, if any, because he received that money as alleged profit sharing when he was not entitled to any profit sharing.

95. Cascade is entitled to recover the $105,000 by which Simpson was unjustly enriched, plus any interest.

COUNT XXI

96. Cascade realleges the allegations contained in paragraphs 1 through 5 and paragraphs 85 through 89.

97. Cascade, as a savings and loan association, is authorized to provide for

pensions, retirement plans and other benefits for its officers in accordance with a plan adopted by its board of directors. RCW 33.16.150.

98. Pursuant to that authorization, Cascade's board of directors adopted a plan of deferred compensation that included a profit sharing component.

99. The allocation of profit sharing to Simpson in 1989 was not in accordance with the plan adopted by the board of directors, thus such allocation was ultra vires.

100. Cascade is entitled to restitution of the $105,000 plus interest, if any, because such constituted an ultra vires allocation.

WHEREFORE, Cascade prays for relief as follows:

1. Judgment against Simpson for the improper personal expenses he charged Cascade or for which he was reimbursed by Cascade, plus interest.

2. Judgment against Simpson in the amount of the income earned by ICI between January 1, 1981, and March 5, 1990, plus interest.

3. Judgment against Simpson in the amount of losses and damages to Cascade as a result of the Previs loan, plus interest.

4. Judgment against Simpson in the amount of $105,000 for his profit sharing allocation in 1989, plus any interest.

5. Judgment against Simpson for Cascade's costs and fees of investigation and bringing this action, including but not limited to attorneys' fees.

6. For such further relief as the court deems proper.

DATED this _____ day of July, 1990.

PRESTON THORGRIMSON
SHIDLER GATES & ELLIS

By_____
Scott A. Milburn
WSBA No. 15355
Attorneys for Plaintiff

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